In the Supreme Court of the United States.

OCTOBER TERM, 1914.

JOHN F. DODGE AND HORACE E. DODGE, appellants,
v.
JAMES J. BRADY, COLLECTOR OF INTERNAL REVENUE.
No. 581.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF MICHIGAN.

MOTION TO ADVANCE.

Comes now the Solicitor General and moves the court to advance this cause for hearing on a day convenient to the court at the next term.

Appellants filed in the district court a bill in equity praying for an injunction to restrain appellee from collecting from appellants surtaxes assessed against appellants under the Income Tax Act of October 3, 1913, on the ground that subdivision 2 of Division A of Section II of said Act is unconstitutional.

A motion by appellants for a preliminary injunction was denied by the district court and after payments by appellants, under protest, of said surtaxes to the Com-

93159—15

missioner of Internal Revenue, they obtained leave to file, and did file, a supplemental bill setting forth the fact of such payment under protest, renewing their averment that that part of the Act herein before mentioned is unconstitutional, and praying, among other things, for a decree against appellee for the amount of the payments so made.

Motions to dismiss both the original and supplemental bills were filed by appellee, which motions were granted, and the district court entered a decree dismissing both bills, the court holding that the above provision of the Income Tax Act is constitutional. From this decree an appeal has been taken to this court.

The case is of importance to the revenues.

Opposing counsel concur.

JOHN W. DAVIS,
Solicitor General.

MAY, 1915.

○

26

Office Supreme Court, U. S.
FILED
SEP 22 1915
JAMES D. MAHER
CLERK

Supreme Court of the United States.

OCTOBER TERM, 1915.

No. 213.

JOHN F. DODGE and HORACE E. DODGE,
Appellants.

vs.

JAMES J. BRADY, Collector of Internal Revenue,
Appellee.

APPEAL FROM DISTRICT COURT OF THE UNITED STATES,
EASTERN DISTRICT OF MICHIGAN.

ADDITIONAL BRIEF ON BEHALF OF APPELLANTS.

WILLIAM D. GUTHRIE,
FRED A. BAKER,
Of counsel for appellants.

INDEX.

	PAGE
Statement	1
Assignment of Errors	5
As to jurisdiction and procedure	7
As to the power of taxation vested in Congress by the Constitution of the United States	10
Analysis of the Federal Income Tax Law of 1913	28
Conclusion	35
Appendix	36

List of Cases.

Barron v. *The Mayor and City Council of Baltimore*, 7 Pet. 243	18
Billings v. *United States*, 232 U. S. 261	11, 13, 15
Campbell v. *Golden Cycle Min. Co.*, 141 Fed. 610	8
Cohens v. *Virginia*, 6 Wheat. 399	14
Corsicana Nat. Bk. v. *Johnson*, 218 Fed. 822	9
County of Santa Clara v. *Southern Pac. R. Co.*, 18 Fed. Rep. 385; 118 U. S. 394	24
Dartmouth College v. *Woodward*, 4 Wheat. 518	19
Eliot v. *Freeman*, 220 U. S. 178	11
Flint v. *Stone Tracy Co.*, 220 U. S. 107	11, 12
Fowler v. *Osgood*, 141 Fed. 20	8
French v. *Barber Asphalt Co.*, 181 U. S. 324	22
Goldschmidt Thermit Co. v. *Primos Chemical Co.*, 216 Fed. 382	9
Goodman v. *Niblack*, 102 U. S. 556	7
Heckscher v. *Penn. Steel Co.*, 205 Fed. 377	9
House v. *Mullen*, 22 Wall 42	7

PAGE

Indian Land & Trust Co. v. *Shoenfelt*, 135 Fed. 484 8
Keith v. *Clark*, 97 U. S. 454 7
Kendig v. *Dean*, 97 U. S. 423 7
Knowlton v. *Moore*, 178 U. S. 41 ..... 15, 16
Lalouj v. *Port of Mobile*, 127 U. S. 640 15
McCoach v. *Minehill Railway Co.*, 228 U. S. 295 11
McCray v. *United States*, 195 U. S. 27 16
McCulloch v. *Maryland*, 4 Wheat. 316 29
Magoun v. *Illinois Trust & Savings Bank*, 170 U. S. 283 .. 29
Monongahela Navigation Co. v. *United States*, 148 U. S. 312 21
Morrison v. *Manchester*, 58 N. H. 538 27
Oliver v. *Washington Mills*, 11 Allen 268 12
O'Neil v. *Wolcott Mining Co.*, 174 Fed. 527 8
Pollock v. *Farmers Loan & Trust Co.*, 157 U. S. 429 ... 11, 14, 26
Prout v. *Starr*, 188 U. S. 537 18
Sjoli v. *Dreschel*, 199 U. S. 564 14
Southwestern Oil Co. v. *Texas*, 217 U. S. 114 23
State v. *Express Co.*, 60 N. H. 219 27
State v. *Township Committee of Readington*, 36 N. J. L. 66 27
Stratton's Independence v. *Howbert*, 231 U. S. 399 ..... 11, 16
Twining v. *New Jersey*, 211 U. S. 78 23
United States v. *Utah Power & Light Co.*, 208 Fed. 821 9
Weyerhaeuser v. *Hoyt*, 219 U. S. 380 14
Wight v. *Davidson*, 181 U. S. 371 22
Zonne v. *Minneapolis Syndicate*, 220 U. S. 187 11

Supreme Court of the United States.

OCTOBER TERM, 1915.

No. 213.

JOHN F. DODGE and HORACE E. DODGE,
Appellants.

versus

JAMES J. BRADY, Collector of Internal Revenue,
Appellee.

APPEAL FROM DISTRICT COURT OF THE UNITED STATES, EASTERN DISTRICT OF MICHIGAN.

ADDITIONAL BRIEF ON BEHALF OF APPELLANTS.

STATEMENT.

The present case, it is understood by counsel, is the first to come before this court involving the exercise of the taxing power by Congress under the authority recently conferred by the Sixteenth Article of Amendment to the Constitution of the United States. The act of Congress of October 3, 1913, known as the Income Tax Law of 1913, 38 Stat. 166, introduces a new and probably permanent system of federal taxation; it contains discriminatory and unjust features, and it presents questions of constitutional law which have not heretofore been determined by the court. The provisions of the act which are deemed pertinent to the present discussion are printed in full in the appendix to this memorandum, but part will be summarized.

The Income Tax Law of 1913 imposes what is termed a

"normal income tax" of one per centum, which is levied and assessed annually upon the entire net income arising or accruing from all sources to every citizen of the United States whether residing at home or abroad, to every person residing within the United States though not a citizen thereof, and to every corporation, joint-stock company or association and every insurance company organized in the United States, no matter how created or organized. The annual profits of all copartnerships, whether or not divided among the copartners, are to be included as part of the taxable income of the individual partners, but the profits of corporations, if undistributed, are not to be so included. From the amount subject to the normal tax each individual is allowed a deduction or exemption of $3,000, plus $1,000 additional if married and living with husband or wife, as the case may be. No deduction or exemption is allowed to corporations. Individuals are allowed to deduct from the amount of income subject to the normal tax all dividends received from corporations, etc., but corporations are not allowed to make any such deduction. Individuals are also allowed to deduct from the amount subject to taxation *all* interest paid by them upon indebtedness, but corporations are only allowed to deduct interest paid on indebtedness to an amount not exceeding one-half of the sum of their interest-bearing indebtedness and their paid-up capital stock. A supertax, termed the "additional tax," is levied upon the income of every individual at progressive rates varying from one per centum upon the amount by which the total net income exceeds $20,000 and does not exceed $50,000 to six per centum upon the amount by which the total net

income exceeds $500,000; but no additional or super-tax is levied upon corporations.

For the purpose of the additional or super-tax individuals must include in their returns of taxable income the share to which they would be entitled of the gains and profits "if divided or distributed, whether divided or distributed or not, of all corporations, joint stock companies, or associations however created or organized, formed or fraudulently availed of for the purpose of preventing the imposition of such tax through the medium of permitting such gains and profits to accumulate instead of being divided or distributed." Stockholders of any corporation, joint stock company, or association not so formed or not fraudulently availed of are not required to include in their returns their proportion of any such gains and profits. The stockholders of the great majority of all corporations, including the corporation from which the appellants receive dividends (p. 17), are thus relieved from the additional or super-tax upon surplus income if such income has not been divided or distributed among them. The act further provides that the fact that any corporation, joint stock company, or association is a mere holding company, or the fact that gains and profits are permitted to accumulate beyond the reasonable needs of the business, is to be prima facie evidence of a fraudulent purpose to escape the tax. The mere fact, however, that the gains are in any case permitted to accumulate and become surplus is not to be construed as evidence of a purpose to escape the tax, unless the Secretary of the Treasury shall certify that in his opinion such accumulation is not reasonable for the

purposes of the particular business. The Commissioner of Internal Revenue, in order to enable him to verify or correct the returns of individuals in these cases, is given power to require a correct statement from any corporation, joint stock company, or association of its profits and the names of the individuals who would be entitled to the same if distributed.

The language of the statute clearly discloses the intention of Congress to provide that the stockholders of corporations, joint stock companies, or associations are to be permitted to accumulate their profits and surplus for the reasonable needs or purposes of the corporate businesses without obligation to pay any additional or supertax thereon, whilst individuals similarly accumulating their profits for the reasonable needs or purposes of their businesses are to be taxed upon such profits and surplus whether the business be conducted individually or in copartnership form. It is also clear that corporations are discriminated against in being taxed upon dividends received from other corporations and in not being allowed to deduct the full amount of interest paid on their indebtedness.

The appellants are and for some years past have been engaged in the business of manufacturing automobile parts in the City of Detroit, Michigan, as copartners under the firm name of Dodge Brothers, and are also interested in a manufacturing corporation (pp. 5, 17). The total amount of net income from gains and profits derived by each from their copartnership business during the ten months from March 1 to December 31, 1913, was $650,888 (p. 7), or $1,301,776 in the aggregate, on which

each was assessed and paid the additional tax of about $28,250, making $56,500 for both partners. If they had been carrying on identically the same business in corporate form and had not divided or distributed the profits, the tax payable by the corporation would have been only one per centum of $1,301,776 of profits, or $13,017. The total amount of net income derived by each appellant from dividends on the stock or from the net earnings of corporations, etc., subject to like tax was $216,941, on which was assessed and paid the additional tax of six per centum, or $13,016.

The above discriminations as between taxpayers are alleged by the appellants to be unreasonable, unjust and arbitrary. The present statute could readily have avoided all the discriminations now complained of (a) by confining the tax to individuals and using the corporation only for the purpose of reaching the source of income, (b) by compelling individual stockholders to return for taxation their share of undivided or undistributed corporate net profits as in the case of copartnerships, and (c) by allowing corporations to deduct from the normal tax all interest paid and dividends received.

ASSIGNMENT OF ERRORS.

1. That if it be held that the court below should have dismissed the bills for want of jurisdiction, then the form of the decree was erroneous.

2. That the Income Tax Law of 1913 is unconstitutional in so far as it discriminates against individuals and copartnerships by imposing the additional or super-tax upon taxpayers carrying on business individually or in

copartnership form and not upon those carrying on business in corporate form.

3. That said Income Tax Law is unconstitutional in so far as it permits those doing business in corporate form to accumulate net profits and surplus free from the additional or super-tax.

4. That said Income Tax Law is unconstitutional in so far as it denies to corporations the right to deduct interest paid and dividends received, which deductions are allowed to individuals.

The appellants' contention on the merits is, briefly stated, that Congress, having determined to levy a direct tax on incomes derived from real and personal property and other sources, was not at liberty to discriminate among taxpayers similarly situated by imposing different rates upon exactly the same kind of income. They submit that if a direct tax is to be levied upon income derived from real or personal property or carrying on business, it cannot be levied at one rate upon the income of individuals or copartnerships and at a different rate upon corporations or those carrying on business in corporate form, and that if deductions are allowed to one or more taxpayers among those selected for taxation, they must be allowed to all in the same class under like conditions. It is contended that this is required not only by the essence and definition of the power to tax, but by the limitations intended to be imposed upon Congress by the Fifth Amendment.

I.

As to jurisdiction and procedure.

The record shows that the court below dismissed the original and supplemental bills upon the merits and not for want of jurisdiction. The decree now before the court, unless reversed, will, therefore, constitute a bar as *res adjudicata* and can be successfully pleaded as such in defense of any action brought at law to recover the taxes paid under protest. The minutes of the proceedings before the court and the final decree (p. 41) expressly declare that the court considered and decided the merits of the controversy, that is, whether the act of Congress of October 3, 1913, was or was not constitutional; and both the original bill and the supplemental bill were thereupon dismissed without reservation. The exception filed by the United States Attorney (p. 45) clearly shows that he understood that the bills were dismissed on the merits. The rule is, of course, well settled that a decree simply dismissing a complainant's bill without saying more, in a case where a dismissal for want of jurisdiction in equity would have been proper and the court in fact intended no more, nevertheless constitutes a bar to any action at law. The practice in such cases is to indicate in the decree that it is not on the merits by stating either that the dismissal is for want of jurisdiction in equity, or that it is without prejudice to an action at law. Where this is not done, appellate courts invariably reverse with direction to enter a proper decree. *House* v. *Mullen*, 22 Wall. 42, 46, 47; *Kendig* v. *Dean*, 97 U. S. 423, 426; *Keith* v. *Clark*, 97 U. S. 454, 456; *Goodman* v. *Niblack*, 102 U. S. 556, 563; *Indian Land &*

Trust Co. v. *Shoenfelt*, 135 Fed. 484, 487; *Fowler* v. *Osgood*, 141 Fed. 20, 24; *Campbell* v. *Golden Cycle Min. Co.*, 141 Fed. 610, 612; *O'Neil* v. *Wolcott Mining Co.*, 174 Fed. 527, 536. If, therefore, it be argued on behalf of the appellee that the court below had no jurisdiction to adjudge the merits, and this contention be approved by the court, the result must in any event be a reversal of the decree now before the court with a direction to the lower court to enter an order transferring the cause to the law side of the court, or else a final decree reciting that the dismissal is for want of jurisdiction or is without prejudice to an action at law to recover the taxes paid under protest as alleged in the supplemental bill (p. 37).

It is, however, submitted on behalf of the appellants that the court below had jurisdiction to hear and determine the merits. As the original and supplemental bills must be read together under the established practice in equity (1 Foster Fed. Practice, 5th edition, p. 765), the cause of action at the final hearing was essentially one to recover the amount of taxes paid under protest. The supplemental bill certainly had no other purpose (p. 37). That an action to recover taxes paid under protest should ordinarily be brought on the law side of the court is not disputed, nor is it disputed that the appellants, after paying the tax under protest, might have discontinued the suit on their original bill instead of filing a supplemental bill, and then have brought their action at law. But whatever may have been the correct practice in this respect prior to the adoption of the new Equity Rules, the procedure in such a case is now regulated by Equity Rule 22, which provides that—

"If *at any time* it appear that a suit commenced

> in equity should have been brought as an action on the law side of the court, it shall be forthwith transferred to the law side and be there proceeded with, with only such alteration in the pleadings as shall be essential."

The inferior federal courts have construed this rule plainly to mean that wherever *at any time* it appears that a litigant is erroneously prosecuting as a suit in equity a controversy only cognizable at law, the court may not dismiss the bill for want of jurisdiction, or because there is an adequate remedy at law, but instead must transfer the case to the law side of the court to be there proceeded with according to the usual practice in cases at law. *Corsicana Nat. Bank* v. *Johnson*, 218 Fed. 822, 823; *Goldschmidt Thermit Co.* v. *Primos Chemical Co.*, 216 Fed. 382, 383; *United States* v. *Utah Power & Light Co.*, 208 Fed. 821, 822; *Heckscher* v. *Pennsylvania Steel Co.*, 205 Fed. 377, 379.

The fact that in the case at bar the circumstances necessary to be averred in order to constitute an action at law were not brought forward until the filing of the supplemental bill seems to us to be immaterial. If the original bill failed to state a cause for either equitable or legal relief, it would have been proper to dismiss it, but before any dismissal took place the facts necessary to constitute a legal cause of action had been brought before the court by supplemental bill duly allowed to be filed (p. 36). At that time it appeared that a legal cause of action was pending before a court of equity, and the trial court was under the duty to give effect to the provision of the new rule 22 by transferring the cause to the law side of the court.

It is further submitted that the appellee cannot success-

fully avail of the fact that the record fails to disclose that there was a transfer to the law side of the court as directed by the rule. It is true and is conceded that no order or record of transfer was made. But there were no disputed facts, and there was nothing for a jury to try. It would consequently have been a useless formality for the court to make an order of transfer. Had the United States Attorney urged or insisted upon a formal transfer of record, the transfer could have been made without in any way changing the forum or the substance of the hearing. The same learned District Judge had jurisdiction at law and in equity, both exercisable in the same tribunal. The trial court was, therefore, entirely justified in proceeding at once to dispose of the merits of the alleged cause of action. Whether the case was one at law or in equity, it presented only a question of law for the court, and, in view of the importance of having constitutional questions involving taxation promptly adjudicated and disposed of, the trial court was right in proceeding directly and promptly to decide the questions raised on the merits.

It is submitted, therefore, that under the supplemental bill the court below had jurisdiction to pass upon the merits of the questions involved in the present litigation.

II.

As to the power of taxation vested in Congress by the Constitution of the United States.

The Income Tax Law of 1894 (Act of Congress of August 27, 1894, 28 Stat. 509, c. 349, s. 27-37) was declared unconstitutional because it was held to be in legal and

practical effect a direct tax upon real and personal property and violated the rule of apportionment among the several States then prescribed in the Constitution of the United States for all direct taxes. *Pollock* v. *Farmers Loan & Trust Co.*, 157 U. S. 429; 158 U. S. 601. The Corporation Tax Law of 1909 (Act of Congress of August 5, 1909, 36 Stat. 11, 112-117, c. 6) was not intended to be and was not in any proper sense an income tax law, but was an excise upon the conduct of business in a corporate capacity. It followed that if a corporation was not actually conducting business, the tax was not payable. *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 142; *Eliot* v. *Freeman*, ibid. at p. 178; *Zonne* v. *Minneapolis Syndicate*, ibid. at p. 187; *McCoach* v. *Minehill Railway Co.*, 228 U. S. 295, 306; *Stratton's Independence* v. *Howbert*, 231 U. S. 399, 414. The same act of Congress contained a tax upon the use of foreign-built yachts, which was likewise sustained as an excise and not as a tax upon property. *Billings* v. *United States*, 232 U. S. 261, 282.

The Sixteenth Amendment was certified to be adopted and in force on and from February 25, 1913. It provides as follows:

> "The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration."

In other words, Congress was granted the express power to levy direct taxes on incomes without being required to apportion them as among the several states. Thereupon, it proceeded to levy such a direct tax on incomes in and by the Income Tax Law of 1913.

The provisions of this Income Tax Law of 1913 do

not differ in substance from those of the prior Income Tax Law of 1894 (U. S. Stat., sec. 27, p. 553); the former levied a tax upon property simply because of its ownership, as the present act does; and hence the act now before the court is to be construed as a direct tax upon income derived from real and personal property and cannot be sustained partly as a direct tax and partly as an excise. The fundamental difference between an excise tax and a direct tax levied on property or income derived from property has been frequently commented upon by writers and courts. Thus, in *Flint v. Stone Tracy Co., supra* (at p. 150, 167), Mr. Justice Day said:

> "The *Pollock Case* construed the tax there levied as direct, because it was imposed upon property simply because of its ownership. In the present case the tax is not payable unless there be a carrying on or doing of business in the designated capacity, and this is made the occasion for the tax, measured by the standard prescribed. The difference between the acts is not merely nominal, but rests upon substantial differences between the mere ownership of property and the actual doing of business in a certain way. . . .
>
> "What we have said as to the power of Congress to lay this excise tax disposes of the contention that the act is void as lacking in due process of law."

In *Oliver v. Washington Mills*, 11 Allen 268, 274, Bigelow, C. J., speaking for the Supreme Judicial Court of Massachusetts, said:

> "An excise, on the other hand, is of a different character. It is based on no rule of apportionment or equality whatever. It is a fixed, absolute and direct charge laid on merchandise, products or commodities, without any regard to the amount of property belonging to those on whom it may fall, or to any supposed relation between money expended for a

public object and a special benefit occasioned to those by whom the charge is to be paid."

This definition of an excise was cited by the Attorney-General of the United States (Hon. Charles Devens) in an opinion furnished Congress for its guidance in April, 1877 (15 Opinions of Attorney-Generals, 219).

The Income Tax Law of 1913 contains novel and unusual provisions and introduces what is generally believed to be a permanent system of federal taxation which is likely to be greatly extended and increased. The assumption of a power in Congress to levy income taxes unrestricted by any constitutional limitations may have led to the present discriminations, and the court is, therefore, urged to permit a renewed discussion and review of some constitutional principles applicable to the power of taxation vested in Congress by the Constitution of the United States.

It is appreciated that in several opinions of the court, and notably in the recent Foreign-Built Yacht Tax Cases (*Billings* v. *United States*, 232 U. S. 261, 282), it has been stated that the authority of Congress to tax is not limited or restricted by the due process of law clause of the Fifth Amendment. But it is, nevertheless, believed to be permissible, in the protection of clients actually discriminated against, to pray the court to reconsider grave questions of constitutional limitations if they are not necessarily precluded by prior decisions. This is particularly true where general language in prior cases may reasonably be said to have been used *arguendo* and not to have been necessary for the disposition of the particular cases before the court. As the late learned

Chief Justice declared in *Pollock* v. *Farmers Loan & Trust Company*, 157 U. S. 429, 576:

> "Manifestly, as this court is clothed with the power, and entrusted with the duty, to maintain the fundamental law of the Constitution, the discharge of that duty requires it not to extend any decision upon a constitutional question if it is convinced that error in principle might supervene."

And as the present learned Chief Justice declared in *Weyerhaeuser* v. *Hoyt*, 219 U. S. 380, 394:

> "If it be conceded that general language was used in the opinion in that case [*Sjoli* v. *Dreschel*, 190 U. S. 564] which when separated from its context and disassociated from the issues which the case involved, might be considered as here controlling, that result could not be accomplished without a violation of the fundamental rule announced in *Cohens* v. *Virginia*, 6 Wheat. 399, so often since reiterated and expounded by this court, to the effect that 'General expressions in every opinion are to be taken in connection with the case in which those expressions are used. If they go beyond the case, they may be respected, but ought not to control the judgment in a subsequent suit when the very point is presented for decision.'"

If, therefore, counsel are convinced that the most serious error in principle would supervene and become established as a binding rule of constitutional interpretation if some of the general expressions of prior opinions were to be taken as controlling and as permitting discriminatory taxation, it surely is their duty on behalf of aggrieved clients to urge their views even though contrary to such general expressions.

No prior case in this court has required an adjudication as to whether or not the Fifth Amendment imposed any restriction upon the taxing power of Congress. The wise

rule of our system of jurisprudence which confines adjudications by the courts to actual cases as they arise from time to time, and to points necessarily involved, has made the growth of American constitutional law extremely slow. It was not for more than a century and until the case of *Knowlton* v. *Moore*, 178 U. S. 41, 92, that the true meaning of the provision that "all duties, imposts, and excises shall be uniform throughout the United States" was definitely settled to require only geographical uniformity. Novel exercises of governmental power frequently require re-examination and renewed exposition of fundamental principles in regard to the powers delegated by the Constitution to the Federal Government. *Ledoup* v. *Port of Mobile*, 127 U. S. 640, 648.

An examination of the cases which are ordinarily cited as establishing the doctrine that Congress may discriminate in taxation and need not observe any rule of equality will show that none of them involved any discrimination among members of the same class of taxpayers.

Thus, in *Billings* v. *United States*, 232 U. S. 261, an excise tax was imposed upon the use of foreign-built yachts but not upon domestic-built yachts, and it could have been upheld as a reasonable classification in the judgment of the court "since," as the opinion declares, "the differences between things domestic and things foreign and their use are apparent on the face of things and are expressly manifested by the text of the Constitution." This conclusion should have disposed of the constitutional point, and the remaining general expressions may, therefore, be regarded as quite unnecessary to the decision.

In *McCray v. United States*, 195 U. S. 27, 61, the classification of oleomargarine as distinct from butter was upheld because of the difference between the two articles not only as a matter of common knowledge but as long recognized in the legislation of Congress and of a majority of the states, and the taxation of colored and uncolored oleomargarine at different rates was held to be justifiable and not arbitrary.

In *Knowlton v. Moore*, 178 U. S. 41, a federal inheritance excise tax was involved which was graduated or progressive, but nevertheless applied without discrimination to all similarly situated. Many writers of recognized authority on political science draw a distinction between inheritance excise taxes levied on the "occasion of a particular isolated act" and direct taxes on property or income, and assert that they differ essentially in nature and permanent incident; but however this may be, there is certainly nothing in *Knowlton v. Moore* to sustain the contention that the tax would have been upheld if the act had discriminated among those inheriting like property of like value under like circumstances.

"As has been repeatedly remarked, the Corporation Tax Act of 1909 was not intended to be and was not in any proper sense an income tax law" (*Stratton's Independence v. Howbert*, 231 U. S. 399, 414); and it was sustained as "an excise tax upon the conduct of business in a corporate capacity." It applied equally to all in the same class carrying on business in like manner.

There is a profound and sincere difference of opinion as to whether it is the true and sound view that Congress has a practical omnipotence in taxation unre-

strained by any constitutional check. On the one hand are those who urge that Congress may discriminate in taxation as greatly as it sees fit, that in the exercise of this legislative power it is not restricted by the provisions of the Fifth Amendment or by any other constitutional limitation except that of apportionment for direct taxes other than income taxes and of geographical uniformity for indirect taxes, and that relief can be granted by the courts in cases involving arbitrary taxation, if at all, only under fundamental conceptions of free government which are said to underlie all constitutional systems. On the other hand are those who urge that Congress in exercising the power of taxation must tax equally all in the same class if in substantially like circumstances and under like conditions, and that the levy of a tax, which is not equal and impartial among members of the same class, is not the exercise of the taxing power but the laying of an arbitrary fine or imposition, or the arbitrary seizure of part of the property of individuals without due process of law and the taking of private property for public use without just compensation. It is further pointed out by the latter that the courts have no power to annul a tax law of Congress simply upon fundamental conceptions of free government and that, therefore, if the express inhibitions of the Fifth Amendment that no person shall be deprived by Congress of his property without due process of law and that private property shall not be taken for public use without just compensation, do not apply at all to the taxing power, the individual would be left without any practical protection whatever against discrimination and oppression by Congress in the exercise of its power to levy taxes.

A.

An examination of the debates in the various conventions to which the Constitution of the United States was submitted for ratification and of the writings of that time will show that federal taxation and the danger of oppression from its exercise were discussed probably more than any other subject. It is well known and this court has recognized that the consent of the people to the adoption of the Constitution in the necessary number of states was secured only upon the pledge that amendments protecting the individual against the abuse of the powers granted to the Federal Government would be forthwith submitted. *Barron* v. *The Mayor and City Council of Baltimore*, 7 Pet. 243, 250. And it was in pursuance of this pledge that the First Congress (1 Stat. 97; Rev. Stat. p. 28 note) proposed the first ten articles of amendment to the Constitution, "in order," as recited in the preamble of the resolution, "to prevent misconstruction or abuse of its powers" and for the purpose of adding "declaratory and restrictive clauses." Of these restrictive clauses, the Fifth Article of Amendment provided that "no person shall . . . . . be deprived of life, liberty or property, without due process of law, nor shall private property be taken for public use without just compensation." These ten amendments have been regarded as of equal force and validity with the provisions of the Constitution itself. *Presser* v. *State*, 188 U. S. 537, 543, 544.

There is no principle of constitutional construction which would permit us to say that if the question of arbitrary or discriminatory taxes could not be shown

to have been in the minds of those who framed and adopted the Fifth Amendment as a limitation upon Congress "in order to prevent misconstruction or abuse of its powers," it cannot now be applied to an abuse of the taxing power as well as to the abuse of any other governmental power. The taxing power was the most important and far-reaching of the powers conferred; it was the one power the absence of which above all others had rendered government under the Articles of Confederation impotent and imbecile; it was the one power most liable to abuse; it was the one power around which waged the contest for ratification of the Constitution, and it was the one which of all powers could most readily be employed against one class of individuals and in favor of another, or to discriminate among members of the same class, if there were to be no restrictions whatever upon its exercise or abuse.

Indeed, even if it could be shown affirmatively that the abuse of the taxing power was not in the minds of the people of the United States at the time the Fifth Amendment was adopted and that the framers apprehended no danger from abuse and discriminations in the exercise of that power, this would not limit the scope of the amendment if the case now presented came fairly within its general spirit and letter. As was said by Chief Justice Marshall in *Dartmouth College* v. *Woodward*, 4 Wheat. 518, 644:

> "It is more than possible, that the preservation of rights of this description was not particularly in the view of the framers of the constitution, when the clause under consideration was introduced into that instrument. It is probable, that interferences of

> more frequent recurrence, to which the temptation was stronger, and of which the mischief was more extensive, constituted the great motive for imposing this restriction on the state legislatures. But although a particular and a rare case may not, in itself, be of sufficient magnitude to induce a rule, yet it must be governed by the rule, when established, unless some plain and strong reason for excluding it can be given. It is not enough to say, that this particular case was not in the mind of the Convention, when the article was framed, nor of the American people, when it was adopted. It is necessary to go farther, and to say that, had this particular case been suggested, the language would have been so varied as to exclude it, or it would have been made a special exception. The case being within the words of the rule, must be within its operation likewise, unless there be something in the literal construction so obviously absurd, or mischievous, or repugnant to the general spirit of the instrument, as to justify those who expound the constitution in making it an exception."

Applying this conclusive reasoning to the federal taxing power, we may well say that there is no reasonable ground which would justify the conclusion that if the abuse of the taxing power by means of unequal and discriminating tax laws had been in the minds of the framers of the Fifth Amendment, they would have varied its language. Had the First Congress deliberated at length upon the choice of a provision which would be more effective than any other to prevent an abuse of the taxing power, it could not have selected one more appropriate than "due process of law." The phrase "due process of law," or its equivalent "the law of the land," long antedated the establishment of our political institutions. It embodied then, as now, the most fundamental and far-reaching maxim of constitutional law and political justice,

and it represented the broadest and most comprehensive guaranty of personal and property rights. In fact, there are no words in our language which signify or mean more in respect of the rights and liberties of the individual.

In *Monongahela Navigation Co. v. United States*, 148 U. S. 312, 324, 336, Mr. Justice Brewer, speaking for the court, used the following language in regard to the power of eminent domain as limited by the Fifth Amendment, and this language it is submitted applies equally to the power of taxation, viz.:

> "Obviously, this question, as all others which run along the line of the extent of the protection the individual has under the Constitution against the demands of the Government, is of importance; for in any society the fulness and sufficiency of the securities which surround the individual in the use and enjoyment of his property constitute one of the most certain tests of the character and value of the government. The first ten amendments to the Constitution, adopted as they were soon after the adoption of the Constitution, are in the nature of a bill of rights, and were adopted in order to quiet the apprehension of many, that without some such declaration of rights the government would assume, and might be held to possess, the power to trespass upon those rights of persons and property which by the Declaration of Independence were affirmed to be unalienable rights. . . . .
>
> "But like the other powers granted to Congress by the Constitution, the power to regulate commerce is subject to all the limitations imposed by such instrument, and among them is that of the Fifth Amendment, we have heretofore quoted. Congress has supreme control over the regulation of commerce, but if, in exercising that supreme control, it deems it necessary to take private property, then it must proceed subject to the limitations imposed by this Fifth Amendment, and can take only on payment of just compensation."

In *French* v. *Barber Asphalt Paving Co.*, 181 U. S. 324, 329, Mr. Justice Shiras, speaking for the court, said:

> "Certainly, it cannot be supposed that, by the Fourteenth Amendment, it was intended to impose on the States, when exercising their powers of taxation, any more rigid or stricter curb than that imposed on the Federal Government, in a similar exercise of power, by the Fifth Amendment."

And in the same case Mr. Justice Harlan dissenting said (at p. 355):

> "As the court expressly declines to formulate any rule to determine for all cases 'what it is for a State to deprive a person of life, liberty or property without due process of law,' I will not enter upon a discussion of that question, but content myself with saying that the prohibition against the deprivation of property without due process of law cannot mean one thing under the Fifth Amendment and another thing under the Fourteenth Amendment, the words used being the same in each Amendment. If the court intends to intimate the contrary in its opinion, I submit that the intimation is not sustained by any former decision, and is not justified by sound principle."

Logically, if in reason there should be any difference, it should exist against the Federal Government, which is indisputably one of limited and enumerated powers. Cooley on Taxation, p. 12.

In the case of *Wight* v. *Davidson*, 181 U. S. 371, 377, the opinion of the court, in referring to a federal statute, declared that "the constitutional right against unjust taxation is given for the protection of private property," but it did not discuss what provision of the Constitution secured that right, although plainly the Fifth Amendment must have been in the mind of the court. Otherwise there was no constitutional right against unjust taxation.

In *Twining* v. *New Jersey*, 211 U. S. 78, 101, Mr. Justice Moody, discussing the "due process of law" provision in the Fifth Amendment, said:

> "If any different meaning of the same words, as they are used in the Fourteenth Amendment, can be conceived, none has yet appeared in judicial decision."

In *Southwestern Oil Co.* v. *Texas*, 217 U. S. 114, 119, Mr. Justice Harlan delivering the opinion of the court and discussing the taxing power of the states, among other things, said:

> "Looking at the clause of the [Fourteenth] Amendment prohibiting the deprivation of property without due process of law, it is to be remembered that the provision to that effect appeared in most of the state constitutions long before the Amendment was adopted, and that principle was accepted everywhere as vital in the American systems of government. But the amendment, although negative in its words, had the effect to incorporate into the fundamental law of each State a rule theretofore prescribed by the Constitution of the United States for the General Government and its agencies. So that prior to the adoption of the Fourteenth Amendment the States were controlled, in imposing and collecting taxes, entirely by their own fundamental law, and if they departed from due process of law in matters involving the deprivation of property the taxpayer injuriously affected by its action could not, *for that reason*, prior to the Amendment, invoke for his or its protection any provision of the Constitution of the United States. But upon the adoption of the Fourteenth Amendment—whatever their own constitutions may then, or have subsequently, declared—the States became bound, as was the United States by the Fifth Amendment, not to deprive any person of property without due process of law. Still it was never contemplated, when the Amendment was adopted, to restrain or cripple the taxing power of the States, whatever the methods they devised for

> the purposes of taxation unless those methods, by their necessary operation, were inconsistent with the fundamental principles embraced by the requirements of due process of law and the equal protection of the laws in respect of rights of property."

In *County of Santa Clara* v. *Southern Pac. R. Co.*, 18 Fed. Rep. 385, 399; affirmed 118 U. S. 394, Mr. Justice Field said:

> "Unequal taxation, so far as it can be prevented, is, therefore, with other unequal burdens, prohibited by the amendment. There undoubtedly are, and always will be, more or less inequalities in the operation of all general legislation arising from the different conditions of persons from their means, business, or position in life, against which no foresight can guard. But this is a very different thing, both in purpose and effect, from a carefully devised scheme to produce such inequality; or a scheme, if not so devised, necessarily producing that result. Absolute equality may not be attainable, but gross and designed departures from it will necessarily bring the legislation authorizing it within the prohibition. The amendment is aimed against the perpetration of injustice, and the exercise of arbitrary power to that end. The position that unequal taxation is not within the scope of its prohibitory clause would give to it a singular meaning. It is a matter of history that unequal and discriminating taxation, leveled against special classes, has been the fruitful means of oppressions, and the cause of more commotions and disturbance in society, of insurrections and revolutions, than any other cause in the world. It would, indeed, as counsel in the *San Mateo Case* ironically observed, be a charming spectacle to present to the civilized world, if the amendment were to read, as contended it does in law: 'Nor shall any state deprive any person of his property without due process of law, *except it be in the form of taxation;* nor deny to any person within its jurisdiction the equal protection of the laws, *except it be by taxation.*' No such

> limitation can be thus ingrafted by implication upon the broad and comprehensive language used. The power of oppression by taxation without due process of law is not thus permitted; nor the power by taxation to deprive any person of the equal protection of the laws."

It is, therefore, submitted that the Fifth Amendment does apply to the exercise of the taxing power by Congress and that any provision of an act of Congress imposing an unequal and discriminatory tax by means of unreasonable and arbitrary selection among those of the class taxed would conflict with the provisions of that Amendment by depriving the individual of property without due process of law or taking private property for public use without just compensation.

B.

However, if it be ruled that the Fifth Amendment imposes no restraint whatever upon Congress in the exercise of its taxing power and that the people of the United States have under this Amendment no protection against the arbitrary abuse of the power of taxation, there still remains the question whether the grant of power to tax does not in and of itself imply the limitation that a tax must necessarily be a common burden equally imposed upon all of the same class, owning the same kinds of property, having the same kind of income, doing the same acts, or exercising the same privileges.

As Judge Cooley said in his work on The General Principles of Constitutional Law, 3d ed., p. 56:

> "Taxes are distinguished from arbitrary levies in that they are laid according to some rule which appor-

tions the burden between the subjects thereof. An exaction which is made without regard to any rule of apportionment is therefore not a tax, and is not within the constitutional authority of the government."

The only power vested in Congress by the Sixteenth Amendment is to levy and collect direct taxes on incomes. The essence, as well as the definition, of a tax requires a common burden to be imposed on all similarly situated. Use has long affixed that limit to the word tax. Impositions upon selected individuals of a particular class or arbitrary discrimination among members of substantially the same class are not taxes. They are fines, or confiscation, or seizure of private property for public use without just compensation, but not legitimate taxation.

In *Pollock v. Farmers Loan & Trust Co.*, 157 U. S. 429, 599, Mr. Justice Field concurring, among other things, said:

> "The inherent and fundamental nature and character of a tax is that of a contribution to the support of the government, levied upon the principle of equal and uniform apportionment among the persons taxed, and any other exaction does not come within the legal definition of a tax.
>
> "This inherent limitation upon the taxing power forbids the imposition of taxes which are unequal in their operation upon similar kinds of property, and necessarily strikes down the gross and arbitrary distinctions in the income law as passed by Congress. The law, as we have seen, distinguishes in the taxation between corporations by exempting the property of some of them from taxation and levying the tax on the property of others when the corporations do not materially differ from one another in the character of their business or in the protection required by the government."

In *State* v. *Express Co.*, 60 N. H. 219, 236, 252, 253, 263, the Supreme Court of New Hampshire said:

> "If, then, equality and justice is the basis of all constitutional taxation, a statute founded on any other principle cannot be upheld. It is true that absolute equality of taxation cannot in all cases, perhaps not in any case, be attained; but if the inequality results from the inherent difficulty in applying the law, and not from the law itself, we cannot declare the law unconstitutional, and arrest the course of legislation . . . . To the extent of its inequality, a disproportional division of public expense is an uncompensated and unauthorized transfer of private property, for a private purpose, from those who bear more than their shares of the common burden to those who bear less than their shares. *Morrison* v. *Manchester*, 58 N. H. 538, 550."

And in the leading case of *State* v. *Township Committee of Readington*, 36 N. J. L. 66, 70, cited in Mr. Baker's brief heretofore filed, the Supreme Court of New Jersey, among other things, said:

> "It is of the very essence of taxation that it should be equal and uniform, and that where the burden is common there should be a common contribution to discharge it. Cooley's Const. Law, 495. . . . A tax upon the persons or property of A, B and C individually, whether designated by name or in any other way, which is in excess of an equal apportionment among the persons or property of the class of persons or kind of property subject to the taxation, is, to the extent of such excess, the taking of private property for a public use without compensation. The process is one of confiscation and not of taxation."

And in Cooley on Taxation, 3d ed., pp. 4, 260, the learned author said:

> "In an exercise of the power to tax, the purpose always is that a common burden shall be sustained by common contributions, regulated by some fixed

general rule, and apportioned by the law according to some uniform ratio of equality. So the power is not arbitrary, but rests upon fixed principles of justice, which have for their object the protection of the taxpayer against exceptional and invidious exactions, and it is to have effect through established rules operating impartially. . . .

"But when, for any reason, it becomes discriminative between individuals of the class taxed, and selects one for an exceptional burden, the tax is deprived of the necessary element of legal equality, and becomes inadmissible. It is immaterial on what ground the selection is made; whether it be because of residence in a particular portion of the taxing district, or because the persons selected have been remiss in meeting a former tax for the same purpose, or because of any other reason, plausible or otherwise; for if the principle of selection be once admitted, limits cannot be set to it, and it may be made use of for the purposes of oppression, or even of punishment."

III.

Analysis of the Federal Income Tax Law of 1913.

The protection of the Fifth Amendment can be given full effect and its restraints enforced, and the power to tax can be construed as inherently implying certain limitations from the very nature of a tax, without in any way crippling the resources of the Federal Government, or interfering with the due exercise of the taxing power by Congress, or with its discretion as to the objects of taxation or the amount or degree of any particular tax. It is because this discretion in taxation as to selection and amount or rate cannot be reviewed by the courts that it has become a truism "that the power to tax involves the power to destroy." All are liable to such destruction if

necessary for the protection or preservation of the Union — individuals and corporations alike must submit to patriotic sacrifice — but the destruction and sacrifice must be of all equally under like conditions, and cannot be by mere arbitrary selection of members of any class.

No dictum in any judicial decision has been more misconstrued than the statement of Chief Justice Marshall in *McCulloch v. Maryland*, 4 Wheat. 316, 431, "that the power to tax involves the power to destroy," nor is there any declaration whose misapplication is more illustrative of the dangers which lurk in a brilliant epigram. This dictum, like other striking phrases of that great jurist, has sometimes been quoted without reference to its context and in support of doctrines which it does not justify. Indeed, since that decision, there has been no arbitrary or unjust exaction or discrimination under the guise or pretext of taxation but that it has been said to be sanctioned by this dictum. It has done incalculable harm, for it has been held up before Congress and state legislatures as placing in their hands unrestrained power to exercise tyranny in the form of a tax law. "How oft the sight of means to do ill deeds makes ill deeds done" (King John, IV, 2). Chief Justice Marshall never meant to say that the taxing power could be arbitrarily exercised to the extent to which his language has been distorted. What he meant was that the degree or rate or reasonableness of any particular tax could not be reviewed by the courts, and not that members of any particular class could be singled out for destruction by discriminatory and unequal taxes.

In *Mauran v. Illinois Trust & Savings Bank*, 170 U. S.

APPENDIX.

Federal Income Tax Law of 1913.

Title of Act.

"An Act to reduce tariff duties and to provide revenue for the Government, and for other purposes, approved October 3, 1913, 38 Stat. 166-181.

"Section II.

"A. Subdivision 1. That there shall be levied, assessed, collected and paid annually upon the entire net income arising or accruing from all sources in the preceding calendar year to every citizen of the United States, whether residing at home or abroad, and to every person residing in the United States, though not a citizen thereof, a tax of 1 per centum per annum upon such income, except as hereinafter provided; and a like tax shall be assessed, levied, collected, and paid annually upon the entire net income from all property owned and of every business, trade, or profession carried on in the United States by persons residing elsewhere."

"Subdivision 2. In addition to the income tax provided under this section (herein referred to as the normal income tax) there shall be levied, assessed, and collected upon the net income of every individual an additional income tax (herein referred to as the additional tax) of 1 per centum per annum upon the amount by which the total net income exceeds $20,000 and does not exceed $50,000, and 2 per centum per annum upon the amount by which the total net income exceeds $50,000 and does not exceed $75,000, 3 per centum per annum upon the amount by which the total net income exceeds $75,000 and does not exceed $100,000, 4 per centum per annum upon the amount by which the total net income exceeds $100,000

and does not exceed $250,000, 5 per centum per annum upon the amount by which the total net income exceeds $250,000 and does not exceed $500,000, and 6 per centum per annum upon the amount by which the total net income exceeds $500,000. All the provisions of this section relating to individuals who are to be chargeable with the normal income tax, so far as they are applicable and are not inconsistent with this subdivision of paragraph A, shall apply to the levy, assessment, and collection of the additional tax imposed under this section. Every person subject to this additional tax shall, for the purpose of its assessment and collection, make a personal return of his total net income from all sources, corporate or otherwise, for the preceding calendar year, under rules and regulations to be prescribed by the Commissioner of Internal Revenue and approved by the Secretary of the Treasury. For the purpose of this additional tax the taxable income of any individual shall embrace the share to which he would be entitled of the gains and profits, if divided or distributed, whether divided or distributed or not, of all corporations, joint-stock companies, or associations however created or organized, formed or fraudulently availed of for the purpose of preventing the imposition of such tax through the medium of permitting such gains and profits to accumulate instead of being divided or distributed; and the fact that any such corporation, joint-stock company, or association, is a mere holding company, or that the gains and profits are permitted to accumulate beyond the reasonable needs of the business shall be prima facie evidence of a fraudulent purpose to escape such tax; but the fact that the gains and profits are in any case permitted to accumulate and become surplus shall not be construed as evidence of a purpose to escape the said tax in such case unless the Secretary of the Treasury shall certify that in his opinion such accumulation is unreasonable for the purposes of the business.

When requested by the Commissioner of Internal Revenue, or any district collector of internal revenue, such corporation, joint-stock company, or association shall forward to him a correct statement of such profits and the names of the individuals who would be entitled to the same if distributed.

"D. . . . . *Provided further*, That any persons carrying on business in partnership shall be liable for income tax only in their individual capacity, and the share of the profits of a partnership to which any taxable partner would be entitled if the same were divided, whether divided or otherwise, shall be returned for taxation and the tax paid, under the provisions of this section, and any such firm, when requested by the Commissioner of Internal Revenue, or any district collector, shall forward to him a correct statement of such profits and the names of the individuals who would be entitled to the same, if distributed:" . . . .

"G. (a) That the normal tax hereinbefore imposed upon individuals likewise shall be levied, assessed, and paid annually upon the entire net income arising or accruing from all sources during the preceding calendar year to every corporation, joint-stock company or association, and every insurance company, organized in the United States, no matter how created or organized, not including partnerships;" etc.

Office Supreme Court, U. S.
FILED
JUN 26 1915
JAMES D. MAHER
CLERK

Supreme Court of the United States

OCTOBER TERM, 1914.

No. 213

JOHN F. DODGE AND HORACE E. DODGE,
APPELLANTS,

vs.

JAMES J. BRADY, COLLECTOR OF INTERNAL REVENUE.

BRIEF FOR APPELLANTS.

FRED A. BAKER,
Counsel for Appellants.
526 Dime Bank Building,
Detroit, Mich.

DETROIT:
Record Printing Co., Free Press Bldg., 11-17 Lafayette Boulevard.
1915.

INDEX

	Pages
Statement of Case	1-10
Constitutional provisions	1
Statutory provisions contained in Section II of the Revenue Act of Congress, approved Oct. 3, 1913, levying an income tax	2-4
Normal tax of 1 per cent on the incomes of individuals	2
Normal tax of 1 per cent on the incomes of corporations	2
Additional and graduated tax on the incomes of individuals	3-4
Returns by, and assessments made against, the plaintiffs	5-6
Proceedings in court below	6-8
Assignments of Error	8-9
Another case	9
Payment under protest, filing supplemental bill, and prayer for judgment under New Equity Rules 22 and 23	10

ARGUMENT.

I. The whole of Subdivision 2, Division A, of Section II of the Revenue Act of Congress of Oct. 3, 1913, is unconstitutional, because of the invalidity of the provisions: (1) subjecting stockholders in corporations, when computing their surtaxes to liability for the gains and profits of the corporations which have not been divided or distributed; (2) vesting in the Secretary of the Treasury an arbitrary power of determining, without notice or a hearing, whether any corporation has accumulated a greater undivided surplus than is reasonable for the needs and purposes of the business; and (3) permitting corporations to accumulate and withhold from surtax taxation such part of their gains and profits as may be reasonably necessary for the needs and purposes of the business, and in not according such great business privilege to individuals and partnerships 11-15

II. The provisions of Subdivision 2 of Division A of Section II of the Revenue Act of Congress of Oct. 3, 1913, levying a graduated surtax on the incomes of individuals in excess of $20,000 without levying the same on the incomes of corporations in excess of $20,000 are unconstitutional and void 16-38

III. Classifying incomes according to their sources and levying different rates on the several classes has objectionable features and consequences which do not pertain to that classification which is permissible in levying duties, imposts and excises .. 38-41

IV. The additional assessment of $13,216.50 against each of the appellants was not authorized by the act, and they are entitled to recover $26,[illegible] even if the surtax assessed on their incomes subject to the normal tax is constitutional 41-42

283, 294. Mr. Justice McKenna pointed out that the wide range of legislative discretion was "not without limitation, of course," and quoted with approval the now classic definitions of the rule which it is submitted apply as well to Congress as to state legislatures, viz., that

> "Clear and hostile discriminations against particular persons and classes, especially such as are of unusual character, unknown to the practice of our governments, might be obnoxious to the constitutional prohibition."

and that

> "In all cases it must appear not only that a classification has been made, but also that it is one based upon some reasonable ground—some difference which bears a just and proper relation to the attempted classification—and is not a mere arbitrary selection."

The late Mr. Justice Brewer dissenting in the same case, said at p. 301:

> "But when a tax law directly, necessarily and intentionally creates an inequality of burden, it then becomes imperative to inquire whether this inequality thus intentionally created can find any constitutional justification."

It is submitted that the act of Congress of October 3, 1913, directly, necessarily and intentionally creates an inequality of burden. It discriminates against individuals in favor of corporations. It groups individuals and corporations as one class and imposes upon all alike a direct income tax of one per centum, and then in the same act imposes a large additional tax upon part of the same class, namely, upon individuals alone. And it allows individuals large deductions from their taxable incomes which it denies to corporations. No reasonable necessity existed or can be suggested for these discriminations, and

there is no justification for any such legislative favoritism and inequality of burden.

Having determined to levy an income tax upon the theory that corporations were to be classed as separate "persons" or entities, Congress should in any event have consistently adhered to that theory in levying the additional or super-tax. The latter tax would then have had to be imposed equally upon corporations and individuals although in practical operation this would have obviously worked great inequalities of burden because in many cases it would have imposed a large additional or super-tax indirectly upon stockholders whose undivided income would not have warranted any such tax. It should then have been recognized that the only consistent and just course was to disregard the corporate form or fiction and, looking to the substance of things, to treat corporations as copartnerships were treated and assess stockholders by the same rate or rule adopted for the assessment of copartners. This was the only basis upon which such a tax could be apportioned with any reasonable degree of equality and justice. In other words, income accruing to individuals from business transacted in corporate form should have been treated as essentially of the same nature as income accruing to them from business conducted individually or in copartnership form, and should have been taxed accordingly.

By levying this income tax directly upon individuals and not at all upon corporations, every feature of discrimination and inequality of the present law would have been readily avoided. As matter of fact, no practical or administrative difficulty could arise if the additional or super-tax were imposed on the net income of all corpora-

tions whether or not divided and distributed among the stockholders, as is done in the case of copartnerships. The amount of such net income must at present be certified and returned for the purposes of the normal corporate tax, and there would be no more difficulty in reaching the additional tax at the source than there is now in reaching at the source all interest paid by corporations, copartnerships, or individuals. The total aggregate of interest payments by corporations undoubtedly much exceeds the aggregate of dividends.

There was, therefore, no reasonable ground or necessity for relieving corporations altogether from the additional tax, and permitting income to be accumulated by corporations for their legitimate needs or purposes and the expansion and development of their businesses freed from the payment thereon of any additional tax, while denying such privilege to those who conduct business as individuals or copartners. The principle of either the stoppage-at-source or the information-at-source is undoubtedly a wise and economical administrative policy, but taxing the corporate source of income without regard to the stockholders must unavoidably and necessarily create arbitrary discriminations such as are now to be found in the Income Tax Law of 1913.

So in regard to interest: corporations are allowed to deduct interest paid on only one-half the sum of their interest-bearing debt and paid-up capital stock, whilst individuals are allowed to deduct all interest paid on borrowed money. This was a compromise, but, as Professor Seligman pointed out in the Political Science Quarterly (vol. 29, p. 10), it is "entirely arbitrary." The tax as it stands unnecessarily discriminates and, more-

over, imposes double taxation. The corporation must pay the normal tax of one per centum upon the surplus interest paid by it and then the individual creditor must again pay not only the normal tax but the additional or super-tax upon the same interest as income. In other words, both the corporate borrower and the lender pay an income tax on such interest as net income. This discrimination and inequality as between individuals and copartnerships on the one hand and corporations on the other could be wholly avoided by allowing a corporation to deduct the interest it paid on borrowed money just as individuals and copartnerships are allowed to do, and then taxing the interest as income, which it indisputably is, of the lender or creditor.

In regard to dividends, there was likewise no reasonable ground either for compelling corporations to pay the normal tax on dividends received from corporations which had already paid such tax as part of their income, or for compelling stockholders to pay an additional or super-tax up to six per centum in case such dividends were distributed among them and no such tax in case the corporation receiving the dividends did not divide or distribute the amount thereof. If, for example, the appellants, Dodge Brothers, had been doing business in corporate form and had collected dividends amounting in the aggregate to $433,882 (pp. 6-7), they would have paid thereon as a corporation only one per centum, or $4,338, whilst as individuals or partners they had to pay practically six per centum, or $26,032.

If Congress should attempt to levy import duties on a particular article and tax importations of such article by corporations at the rate of one per centum *ad valorem*

and importations by individuals at six per centum, or *vice versa*, would this be held to be a valid excise tax? The act or privilege taxed would be identically the same in each case, namely, the importation of a foreign article. Could it then be successfully argued in support of any such legislation that the tax was within the discretion of Congress and that no power existed in the courts to grant relief to those who were discriminated against?

Again, Congress might decide to levy an excise tax on the manufacture of whiskey, or beer, or tobacco, and tax corporations at the rate of one per centum of their gross or net income and individuals at the rate of six per centum for doing exactly the same act or exercising the same privilege. Would such a discrimination against individuals be constitutional; and if not, on what grounds could the courts give relief, if not under the Fifth Amendment?

It is true that a separate excise tax might have been levied on the doing or carrying on of business in corporate form or capacity, as was the case in the Corporation Tax Law of 1909. But this was not done. The present tax is radically different from the excise tax of 1909, but similar to the direct income tax of 1894. It is a direct tax on income from property or whatever other source derived, and it does not purport to be and is not an excise tax on the privilege of doing business in corporate form or capacity. A tax plainly intended by Congress to be a direct tax on income from property cannot be turned by judicial interpretation into an indirect excise on the privilege of carrying on business in corporate capacity in order to sustain a discrimination in favor of

corporations. Nothing in the act would justify the assumption that Congress had entertained any such intention, or intended to levy any such excise tax. It is highly probable that if Congress had realized that in levying direct taxes on incomes it could not discriminate as among taxpayers subjected to the tax or favor corporations as against individuals, or *vice versa*, it would have so remodelled the statute as to tax stockholders individually upon their interests in the undistributed profits of corporations and would have equalized the deductions, thereby reaching all individual incomes alike whether arising or accruing from corporations, copartnerships, or individual holdings.

CONCLUSION.

For the reasons stated above, it is submitted that the provisions of the Federal Income Tax Law of 1913, which levy the additional or super tax on individuals and which deny to corporations deductions of interest and dividends allowed to individuals and copartnerships, are unreasonably and arbitrarily discriminatory and as such are not legitimate taxation, and, therefore, violate the prohibitions of the Fifth Amendment to the Constitution of the United States by depriving taxpayers of property without due process of law and by taking private property for public use without just compensation.

September 21, 1915.

WILLIAM D. GUTHRIE,
FRED A. BAKER,
Of counsel for appellants.

July 1, 1914, a memorandum was filed stating the granting of the motion to dismiss, with this conclusion:

> "The court stated that after examining the authorities he was of the opinion that the law was constitutional." (*Record, pp.* 40-41.)

Assignments of Error.

The assignments of error filed with the petition for appeal contains eight assignments. (*Record, p.* 43.)

As they are all relied on they are here inserted:

1. The court erred in refusing to grant the temporary injunction prayed by the plaintiffs and in denying the motion of the plaintiffs for an injunction restraining the defendants from collecting the surtaxes assessed against them in their income tax assessments.
2. The court erred in holding that subdivision 2 of Division A of section 2 of the revenue act of Congress of October 3, 1913, is constitutional and valid.
3. The court erred in granting the motions of the defendant to dismiss the original and supplemental bills of the plaintiffs.
4. The court erred in holding that section 3224 of the Revised Statutes of the United States applies to the case of the plaintiffs.
5. The court erred in refusing to hold that if said section 3224 applies to the case of the plaintiffs, it is to the extent of such application unconstitutional and void, because in conflict with the provision of the Constitution of the United States that the judicial power of the United States in cases at law and in equity, is vested in the Supreme Court of the United States and in such inferior courts as may be created by Congress.
6. The court erred in refusing to hold that the said subdivision 2 of Division A of section 2 of the Revenue Act of Congress of Oct. 3, 1913, and the surtaxes levied thereunder are in conflict with the provisions of the Fifth Amendment of the Constitution of the United States that no person shall be deprived of life, liberty or property without due process of law, and that private property shall not be taken for the public use without just compensation.
7. The court erred in holding that the surtax on

the alleged income of $220,275 at the rate of 6% assessed against each of the plaintiffs is within said subdivision 2 and is authorized by the same.

8. The court erred in refusing to render a decree and judgment in favor of the plaintiffs and against the defendant for the recovery of the surtaxes so assessed against them, and paid by them under protest as set forth in their said supplemental bill.

ANOTHER CASE.

The protest submitted with, and the further protest and request for a hearing contained in the letter to the Commissioner of Internal Revenue, were submitted to the Hon. William H. Osborne in person on the 13th day of March, 1914, and the hearing denied. (*Record, pp.* 8-13.)

On the 16th day of March, 1914, the appellants filed a bill in equity in the Supreme Court of the District of Columbia, praying for a temporary and perpetual injunction enjoining the Commissioner from making any *assessment* of surtaxes against them.

That court, Hon. Wendell P. Stafford, justice, denied a motion for an injunction and granted a motion to dismiss the bill.

An appeal was taken to the Court of Appeals of the District of Columbia, where the decree below dismissing the bill was affirmed in an opinion by Mr. Justice Van Orsdel.

Neither of these courts passed upon the question whether the surtax provisions of the income tax law are valid, but held that under the legislation of Congress a bill for an injunction could not be sustained.

Appellants took and perfected an appeal to the Supreme Court of the United States, and the case is No. 871 on the October, 1914, docket.

The Present Case.

In the present case the question whether the appellants were entitled to injunctive relief has been partly eliminated by the circumstance, that failing to obtain an injunction in the court below, the appellants paid the surtaxes assessed against them under duress and process, and then by leave of the court filed a supplemental bill, praying under new equity rules 22 and 23, for a judgment against the collector for the recovery of the money so paid by them.

Their appeals or claims for the abatement and remission of the surtaxes having in the meantime been denied by the Commissioner of Internal Revenue, it was not necessary for them to file a claim to have the money paid refunded, under 3220 of the Rev. Stat., before bringing suit. The moment they paid their surtax assessments under protest, they were at liberty to bring actions at law against the collector for the recovery of their money. *Schwerzchild & Sulsberger vs. Rucker*, 143 *Fed.*, 656; *Grier vs. Tucker*, 150 *Fed.*, 658, *De Barry vs. Dunne*, 162 *Fed.*, 961.

New Equity Rules.

22. If at any time it appear that a suit commenced in equity should have been brought on the law side of the court, it shall be forthwith transferred to the law side and be there proceeded with, with only such alteration in the pleadings as shall be essential.

23. If in a suit in equity a matter ordinarily determinable at law arises, such matter shall be determined in that suit according to the principles applicable, without sending the case or question to the law side of the court.

In the present case no change in the pleadings was essential, and no reference of the case to the law side of the court was necessary, because the supplemental bill set up the additional facts and prayed for a decree according to the provisions of Sec. 3220 Rev. Stat. U. S., and new Federal Equity Rules No. 22 and 23. (*Record, pp.* 37-38.)

We think we have made a correct and sufficient statement of this case.

In the present brief we will only consider the constitutional questions involved, and will reserve the question whether the appellants were entitled to injunctive relief for consideration in a brief entitled in the other case.

I.

The whole of Subdivision 2, Division A, of Section II of the Revenue Act of Congress of Oct. 3, 1913, is unconstitutional, because of the invalidity of the provisions: (1) subjecting stockholders in corporations, when computing their surtaxes to liability for the gains and profits of the corporations which have not been divided or distributed; (2) vesting in the Secretary of the Treasury an arbitrary power of determining, without notice, or a hearing, whether any corporation has accumulated a greater undivided surplus than is reasonable for the needs and purposes of the business: and (3) permitting corporations to accumulate and withhold from surtax taxation such part of their gains and profits as may be reasonably necessary for the needs and purposes of the business, and in not according such great business privilege to individuals and partnerships.

Very little need be said about the provision which provides that stockholders in corporations may be assessed a surtax on the corporate gains and profits which have not been distributed in dividends, but have been allowed to accumulate as surplus, and be used in the business, and have not been and may never be distributed in dividends.

The act contains no machinery or means of compelling a corporation (and there is none elsewhere) to pay dividends when it does not wish to do so.

To tax a stockholder on prospective dividends which he may never receive can only be properly characterized as so utterly absurd as to induce levity. Individuals are taxed on their gains and profits whatever disposition they may make of them, and corporations may be taxed on their gains and profits whether divided and distributed or not; but if a stockholder has not received his share of the undivided profits, and the corporation is allowed to retain them in its business and not pay any surtax thereon, it is not thinkable that the stockholder may be compelled to pay an income tax on his share of the withheld gains and profits of the corporation.

It is provided that the fact

> "that the gains and profits are permitted to accumulate beyond the reasonable needs of the business shall be *prima facie* evidence of a fraudulent purpose to escape such tax."

But who is to determine the fact whether the accumulation is beyond the reasonable needs of the business? When and on what notice and hearing is the fact to be determined?

Division G (*c*) of the law, fixing the taxation, and the items of the returns of corporations, does not require them to set forth the dividends paid during the year or the surplus accumulated, but does require them to set forth their gross income and after making the deductions enumerated, their net income.

This probably explains why the last clause of Subdivision 2 of Division A provides:

> "When requested by the Commissioner of Internal Revenue or any district collector of internal revenue, such corporation, joint stock company or association shall forward to him a correct statement of such profits and the names of the individuals who would be entitled to the same if distributed."

With such a statement before him the Commissioner of Internal Revenue would know that a surplus had been accumulated, and the mere fact of its accumulation would be *prima facie* evidence of a fraudulent purpose, according to one clause, and according to the succeeding clause:

> "Shall not be construed as evidence of a purpose to escape such tax unless the Secretary of the Treasury shall certify that in his opinion such accumulation is unreasonable for the purposes of the business."

If the Secretary of the Treasury should in any case so certify would it be incumbent on him to determine the extent to which the accumulation was in his opinion unreasonable, and the extent to which in his opinion it was reasonable, or would his certificate that the accumulation was unreasonable make it the duty of the Commissioner of Internal Revenue, in assessing the stockholders of the corporation for their surtaxes to charge them with their respective shares of the *whole* of the accumulation retained as surplus and not distributed by the corporation among them.

In computing the incomes of the stockholders for the purposes of the normal tax, they are authorized in their returns to deduct as the seventh deduction from their gross incomes,

> "the amount received as dividends upon the stock or from the net earnings of any corporation, joint stock company, association, or insurance company which is taxable upon its net income as hereinafter provided." (See Division B of the law.)

This shows that dividends actually received during the year are deducted in computing the normal tax, and that under subdivision 2 of Division A the dividends so received are put back into the taxable income in computing the surtax.

We have not been able to discover the object of this transmution of income from the one tax to the other; but it does show a line of demarkation between dividends actually received and the shares of the stockholders in the gains and profits of a corporation, which were not divided or distributed but accumulated as surplus.

The statements furnished the Commissioner by corporations (under the last clause of Subdivision 2 of Division A, quoted above), will show the undivided gains and profits, carried as "surplus" or "undivided profits," but the fact that they have been

> "permitted to accumulate and become surplus shall not be construed as evidence of a purpose to escape said tax in such case unless the Secretary of the Treasury shall certify that in his opinion such accumulation is unreasonable for the purposes of the business."

The Commisioner is under no obligation to call for a statement from any corporation, and the Secretary of the Treasury is under no duty or obligation to certify his opinion.

All which shows that corporations, at the discretion of the Commissioner of Internal Revenue and the Secretary of the Treasury may withhold from the surtax taxation of their stockholders such portion of their gains and profits as may please them, whether necessary for the purposes of the business or not, unless the Secretary of the Treasury interposes his opinion that the accumulation in any case is unreasonable for the purposes of the business.

Nearly all corporations do retain a portion of their gains and profits, and do not distribute such portions among their stockholders, and this law permits them to do so, subject to the opinion of the Secretary of the Treasury.

Individuals and partnerships are not accorded any such privilege, so that their corporation competitors in business are given a great advantage over them which is of supreme importance in a growing and expanding business, requiring large additional investments of capital, which must come from accruing gains and profits or from new stock subscriptions or bonded indebtedness. A more invidious and objectionable discrimination from a business standpoint is not conceivable.

The foregoing analysis of the surtax provisions of the income tax law of 1913 makes the following propositions, whatever may be their legal consequences, absolutely true:

1. Stockholders in corporations are taxed on dividends they have not received and may never receive.

2. The Secretary of the Treasury, without notice or a hearing, is given the arbitrary power of determining whether the undivided gains and profits of corporations have been accumulated beyond the reasonable needs of the business.

3. Corporations are permitted, unless the Secretary of the Treasury interposes his opinion to the contrary, to withhold from the surtax taxation of their stockholders, a portion of their gains and profits, while no such permission is granted to individuals and partnerships.

Neither of these three propositions can be sustained as good constitutional law.

First. That a tax can be levied on incomes not received and may never be received, is an absurdity.

The only instance in which one person can be compelled to pay another person's tax is found in the law of some of the states that when a tax collector goes to collect a tax by a distraint of personal property, he is at liberty to seize and sell any personal property he may find in the possession of the delinquent, wholly regardless of its ownership.

Such a law was sustained by the Supreme Court of Michigan in *Sears vs. Cottrell*, 5 *Mich.*, 251; but we call attention to the dissenting opinion of Justice Campbell, who reaches the conclusion that such a law goes beyond constitutional limits.

Be that as it may be, it is a self-evident proposition that a person can not be assessed for taxes on property which he does not own and of which he has no possession.

Second. That the Secretary of the Treasury cannot be authorized to determine without notice or a hearing whether a corporation has accumulated a surplus in excess of the needs and purposes of the business, has been conclusively established by repeated decisions of this court, which were recognized and enforced by the court in the very recent case of *Coe vs. Armour Fertilizer Works*, 35 *Sup. Court Reporter*, p. 625, decided May 3, 1915.

The court cited and approved the following cases in which it was held that statutes are unconstitutional if they do not provide for notice and a hearing. *Stuart vs. Palmer*, 74 *N. Y.* 183, 188; *Security Trust & S. B. Co. vs. Lexington*, 203 *U. S.*, 323, 333; *Georgia R. Co. vs. Wright*, 207 *U. S.*, 127, 138; *Roller vs. Holly*, 176 *U. S.*, 398, 409; *Louisville & N. R. Co. vs. Central Stock Yards*, 212 *U. S.*, 132, 144.

Third. That corporations by the exercise of executive discretion may be permitted to accumulate gains and profits reasonably necessary for the needs and purposes of the business, and individuals and partnerships be denied such privilege, is beyond any classification for the purposes of taxation, that has ever been sustained, outside of duties and excises, which are in their nature specific discriminations.

The subject of classification for the purposes of taxation or legislation will be more fully considered in the next subdivision of this brief.

The three extraordinary provisions to which we have called attention are material and component parts of the scheme of surtax taxation of subdivision 2 of Division A of the income tax law, and to strike them out would leave said subdivision so emasculated and deformed that it is not believable that Congress would have passed it in the condition the constitution compels the court to leave it. The case is controlled by *Pollock vs. Farmers' Loan & Trust Co.*, 158 *U. S.*, 601, wherein the entire income tax law of 1894 was declared void because of the invalidity of a part of it.

STATUTORY PROVISIONS.

Section II of the Revenue Act of Congress approved Oct. 3, 1913, is an income tax law (38 U. S. Stat., 166-181).

Division A, Subdivision I:

> "That there shall be levied, assessed, collected and paid annually upon the entire net income arising or accruing from all sources in the preceding calendar year to every citizen of the United States, whether residing at home or abroad, and to every person residing in the United States though not a citizen thereof, a tax of 1 per centum per annum upon such income, except as hereinafter provided; and a like tax shall be assessed, levied, collected, and paid annually upon the entire net income from all property owned and of every business, trade, or profession carried on in the United States by persons residing elsewhere."

Division G (*a*) says:

> "That the normal tax hereinbefore imposed upon individuals likewise shall be levied, assessed and paid annually upon the entire net income arising or accruing from all sources during the preceding year to every corporation, joint stock company or association, and every insurance company organized in the United States, no matter how created or organized, not including partnerships;" etc.

Division D contains the following provision:

> "That any persons carrying on business in partnership shall be liable for income tax only in their individual capacity, and the share of the profits of a partnership to which any taxable partner would be entitled if the same were divided, whether divided or otherwise shall be returned for taxation and the tax paid under the provisions of this section."

The normal tax of one per centum is levied on the net incomes (less the exemptions and deductions allowed by other provisions of the law) of all individuals and corporations doing business for gains and profits in the United States, without any discrimination as between natural persons and artificial persons.

The provisions the constitutionality of which is denied by the appellants are contained in

SUBDIVISION 2 OF DIVISION A.

"*Subdivision 2. In addition to the income tax provided under this section (herein referred to as the normal income tax) there shall be levied, assessed and collected upon the net income of every individual an additional income tax (herein referred to as the additional tax) of*

1 per centum per annum upon the amount by which the total net income exceeds $20,000 *and does not exceed* $50,000, *and*

2 per centum per annum upon the amount by which the total net income exceeds $50,000 *and does not exceed* $75,000,

3 per centum per annum upon the amount by which the total net income exceeds $75,000 *and does not exceed* $100,000,

4 per centum per annum upon the amount by which the total net income exceeds $100,000 *and does not exceed* $250,000,

5 per centum per annum upon the amount by which the total net income exceeds $250,000 *and does not exceed* $500,000, *and*

6 per centum per annum upon the amount by which the total net income exceeds $500,000.

"All the provisions of this section relating to individuals who are to be chargeable with the normal income tax, so far as they are applicable and are not inconsistent with this subdivision of paragraph A, shall apply to the levy, assessment and collection of the additional tax imposed under this section.

"Every person subject to this additional tax shall, for the purpose of its assessment and collection, make a personal return of his total net income from all sources, corporate or otherwise, for the preceding calendar year, under rules and regulations to be prescribed by the Commissioner of Internal Revenue and approved by the Secretary of the Treasury.

"*For the purpose of this additional tax the taxable*

income of any individual shall embrace the share to which he would be entitled of the gains and profits, if divided or distributed, whether divided or distributed or not, of all corporations, joint-stock companies, or associations however created or organized, formed or fraudulently availed of for the purpose of preventing the imposition of such tax through the medium of permitting such gains and profits to accumulate instead of being divided or distributed.

"And the fact that any such corporation, joint-stock company, or association, is a mere holding company, or that the gains and profits are permitted to accumulate beyond the reasonable needs of the business shall be prima facie evidence of a fraudulent purpose to escape such tax; but the fact that the gains and profits are in any case permitted to accumulate and become surplus shall not be construed as evidence of a purpose to escape the said tax in such case unless the Secretary of the Treasury shall certify that in his opinion such accumulation is unreasonable for the purposes of the business.

"When requested by the Commissioner of Internal Revenue, or any district collector of internal revenue, such corporation, joint-stock company, or association shall forward to him a correct statement of such profits and the names of the individuals who would be entitled to the same if distributed."

The main question in this case is whether the first part of the subdivision, printed in italics, levying a surtax on the incomes of individuals (and not on corporations), exceeding $20,000 is not unconstitutional and invalid, because of the discrimination in favor of corporations and partnerships and against individuals.

This question may not be reached if the whole subdivision must be declared invalid, because of the invalidity of the second part of the subdivision, printed in italics. In the brief which is to follow we will consider that question first, but before proceeding to the legal argument we will state

The Case of the Plaintiffs.

John F. Dodge and Horace E. Dodge are brothers who have for some years been doing business as a partnership under the firm name of Dodge Brothers (*Record, pp.* 1-2).

Upon blanks furnished to them by the Collector of Internal Revenue for the First District of Michigan, they each made a return showing a taxable net income for the year ending December 31, 1913, for John F. Dodge of $708,229.47, and for Horace E. Dodge of $709,243.41, or a total of $1,417,472.88 (*Record, pp.* 2-4).

The normal tax of John F. Dodge was $7,082.29 and of Horace E. Dodge $7,092.43: making a total for both of $14,174.72 (*Record, p.* 13).

They were each assessed a surtax on the income on which was assessed the normal tax of 1 per centum, thus:

John F. Dodge	$32,543.77
Horace E. Dodge	32,604.60
	$65,148.37

Their returns showed that each had received dividends from corporations subject to the like normal tax of $216,941.66. To this was added the statutory exemption of $3,333.34, making the sum of $220,275.00 on which each was assessed a surtax of 6 per centum, amounting to $13,216.50.

The total surtax assessed against John F. Dodge was $45,760.27, and against Horace E. Dodge, $45,821.10. The total amount in controversy on this record is $91,581.37 and interest. (*Record, pp.* 13, 37.)

Each of the appellants annexed to and filed with his return, Feb. 16, 1914, a protest on the ground that the surtax provisions of the Act of Oct. 3, 1913, are unconstitutional and void. The provisions of the constitution of the United States claimed to be violated are specifically stated. (*Record, pp.* 8-9.)

Subsequently each of the appellants submitted to the Commissioner of Internal Revenue in person a letter in which

the objections to the validity of Subdivision 2 of Division A of Section II of the Act of Oct. 3, 1913, are stated in detail. A request was made for a hearing. (*Record, pp.* 10-12.)

Without giving any hearing the Commissioner of Internal Revenue, May 1, 1914, made his assessments against the appellants as above stated. (*Record, p.* 14.)

The Collector of Internal Revenue for the First District of Michigan, May 8, 1914, mailed a notice to each of the appellants, stating that the assessment against John F. Dodge was $52,842.56, and against Horace E. Dodge, $52,863.53, and notifying them that

> "This tax is due and payable on or before June 30, 1914,"

and

> "To avoid penalty and interest taxes must be paid to the collector or person designated by him in such a manner as will enable him to place the same with his depository and receive a certificate of deposit therefor not later than the close of business of the date mentioned in the body of this notice." (*Record, p.* 14.)

The appellants, May 20, 1914, filed with the collector, appeals or claims for the remission and abatement of the surtaxes so assessed against them. (*Record, pp.* 15-16.)

The appellants, June 2, 1914, paid the normal tax assessed against them. (*Record, p.* 16.)

The appellants, June 9, 1914, filed the bill of complaint in this cause. (*Record, pp.* 1-31.)

Proceedings in Court Below.

The appellants, June 11, 1914, filed, with proof of service, a motion for a temporary injunction restraining and enjoining the collector until the further order of the court from collecting or attempting to collect from the plaintiffs or either of them the surtaxes so assessed against them. (*Record, p.* 34.)

The appellants, June 22, 1914, filed with proof of service, a motion for leave to file a supplemental bill. (*Record, p.* 35.)

The motion for a temporary injunction was denied June 29, 1914, and leave to file a supplemental bill was granted. (*Record, p.* 36.)

The supplemental bill was then filed alleging the following facts as having occurred after the original bill was filed. (*Record, pp.* 37-38.)

1. That the appeals or claims of the appellants for the remission and abatement of the surtaxes were denied by the Commissioner of Internal Revenue June 15, 1914.
2. That on June 29, 1914, the court having refused an injunction, the appellants had paid to the collector under duress and protest the said surtaxes.

Thereupon the district attorney, Mr. Clyde I. Webster, as counsel for the collector, filed a motion to dismiss the original and supplemental bills. (*Record, pp.* 38-39.)

The motion was submitted to the court; and the court being of the opinion that the provisions of subdivision 2 of Division A of the Revenue Act of Congress of October 3, 1913, levying additional taxes on the incomes of individuals is constitutional, and

> "that said subdivision is constitutional granted and entered a decree dismissing the original and supplemental bills." (*Record, p.* 41.)

Appellants immediately filed a petition for the allowance of an appeal to the Supreme Court of the United States. The appeal was allowed and the appeal bond fixed at $500. (*Record, p.* 44.)

The bond was filed and approved June 30, 1914. (*Record, p.* 45.)

On the same day the District Attorney filed an exception on the ground that the order of dismissal should not have stated the ruling of the court on the constitutionality of the surtaxes and of said subdivision 2. (*Record, p.* 45.)

The reason for this is, that if the tax is laid on the rents or rental value of real estate, or on the gains and profits derived from personal property, it would in each case be a direct tax, and as such prohibited by the constitution as construed by the Supreme Court of the United States.

Hence the consequent truth, that an Act of Congress classifying incomes by dividing them into two classes with different rates, one class consisting of incomes derived from the gains and profits of corporations as artificial persons, and the other consisting of incomes derived from the gains and profits of individuals as natural persons, the tax is a discriminating tax on the sources of the income or, what is the same thing, on the means or agencies by which the gains and profits were earned.

Some minds are incapable of grasping the distinction on which classifications for the purposes of taxation are to be regarded as valid or invalid. It all depends on what is being taxed. A tax on incomes under the Sixteenth Amendment is not a tax on the property, real or personal, or on the business or vocation, from which the incomes are derived.

Congress can levy a graduated tax on incomes, classifying them according to the amounts of the incomes, with a different rate for each class; but Congress cannot say that incomes from real estate shall pay one rate, and from personal property another rate, and from the manufacturing business another rate, and from the banking business another rate, and from the legal profession another rate, and from the medical profession another rate, and so on to the large number of classifications to which resort might be made, if Congress can lay one rate on incomes earned by individuals and another rate on incomes earned by corporations.

2. Our next objection to the surtax provisions of the income tax law of 1913 is that they violate the provisions of the Fifth Amendment, that no person shall be deprived of life, liberty or property without due process of law, and that private property shall not be taken for public use without just compensation.

These two provisions supplement each other. Taxing or taking private property for a private purpose or use, or taking private property for the public use or benefit without just compensation, is a deprivation of property without due process of law.

It is mathematically demonstrable that the unequal and unjust apportionment of taxation caused by the surtax provisions of the income tax law of 1913 is taxation for a private purpose.

One per centum of the incomes of individuals and corporations produces, say from individuals, $40,000,000, and from corporations $40,000,000, or an aggregate of $80,000,000.

But $20,000,000 more is needed, and if the tax on both individuals and corporations was increased one-quarter of one per cent each would be required to pay $10,000,000. Instead of doing this the surtax provisions of this Act of Congress relieves corporations of their just part thereof, and places it on individuals; that is to say, individuals are required to pay taxes *to pay the taxes of corporations.*

Under pretense of levying taxes for the support of the government, Congress, as a matter of fact, levies taxes on a portion of its taxpayers to pay the taxes in part of another portion of its taxpayers.

Statistics may falsify, but the science of numbers does not.

Taxing one or a number of persons to pay the taxes of other persons is taxation for a private purpose, and a plain violation of the due process clause of the Fifth Amendment.

The reports of the Commissioner of Internal Revenue covering the year 1913 (10 months) shows that the normal tax on individuals amounted to $12,728,038.02, and on corporations $32,456,662.67, making a total of $45,184,700.69. In addition to this the surtaxes of individuals amounted to $15,525,496.83, which could have been raised by increasing the normal tax a little more than one-third of 1 per cent.

The taxes of individuals would have thereby been increased (omitting the small fraction) from $12,728,038.02 to $16,970,717.36, and those of corporations from $32,456,662.67 to $43,275,550.12, or an increase of $10,818,887.55.

That amount was added to the taxes of individuals, in addition to their proper share of the additional money raised by surtaxes. Under this law there was added to the proper share of individuals $10,818,887.55, which was justly and equitably assessable to corporations.

These surtax provisions are so framed that they relieve corporations of a part of their public burdens and places it on individuals, and any argument tending to show that this is taxation for a public purpose must be fallacious.

Corporations organized and conducted for gains and profits are mere private enterprises.

Taxation for their relief or benefit cannot under our American constitutions be sustained, because it takes the property or money of one person and gives it to another, and is not due process of law.

3. Our third objection to the validity of the surtax provisions of the income tax law of 1913 is that they are not within the power of Congress to levy taxes, duties, imposts and excises, or taxes upon incomes from whatever source derived, and are a violation of the Tenth Amendment of the Constitution of the United States, reserving to the states respectively, or to the people, all powers not delegated to the United States.

We would insist on this objection if there was no due process clause in the Fifth Amendment, because there are certain inherent limitations in all systems of constitutional government.

The people of the United States are not divided into three different estates, such as prevailed in England during the Anglo-Norman period, consisting of the baronage, the church, and the commons, among which different rates of feudal dues and taxes obtained.

There can be no such thing in the United States as one estate consisting of corporations and another consisting of individuals.

In the courts of the District of Columbia the counsel for the Commissioner of Internal Revenue failed to comprehend the objections we make to the constitutionality of the surtax provisions of the income tax law.

We do not base our objections on the discrimination against partnerships and in favor of corporations. Partnerships as such are not subjected to either the normal tax or the surtax.

The individuals who are members of a firm of co-partners are assessed and taxed on their several shares of the gains and profits of the firm. In that way the net income of a partnership is reached, but in no other way.

The discrimination is against individuals as natural persons and in favor of corporations as artificial persons.

There is a discrimination in favor of partnerships and against individuals, which is of the same nature as the discrimination against individuals and in favor of corporations. Partnerships are not treated as single entities, doing business as single units, in competition with individuals engaged in the very same business. The discrimination in favor of partnerships and against individuals is more marked than in the other case, because corporations on their net incomes are assessed for the normal tax of one per centum and partnerships are not assessed for either the normal tax or the surtax.

The net incomes of partnerships as single business units are not taxed at all, while the net incomes of corporations only escape the surtax.

There are many single individuals in the United States who conduct large and successful business enterprises for the gains and profits to be realized therefrom, and they may very well object to the discrimination against individuals and in favor of both partnerships and corporations. The present plaintiffs and appellants are partners, and they object to the surtax as a discrimination against them as individuals and in favor of corporations. Their objection is to the surtax and not to the normal tax.

Another misapprehension of the learned counsel is their assumption that we contend that duties, imposts and excises must be not only territorially uniform throughout the United States, but also uniform among the various things and persons subjected to such burdens and charges. We make no such contention. Duties, imposts and excises may be laid at different rates for each of the *many classes* of things or persons as are in existence. The corporation tax of 1909 is a noted recent instance of this power of Congress.

The corporation tax was sustained as an excise and not as an income tax. *Flint vs. Stone-Tracy Co.*, 220 *U. S.*, 107; *United States vs. Whitridge*, 231 *U. S.*, 144.

In *Stratton's Independence vs. Hobart,* 231 *U. S.*, 414, the court said:

> "As has been repeatedly remarked, the Corporation Tax Act of 1909 was not intended to be and is not in any proper sense an income tax law. The court had decided in the *Pollock Case* that the income tax law of 1894 amounted in effect to a direct tax upon property, and was invalid because not apportioned according to population as prescribed by the Constitution. The act of 1909 avoided this difficulty by imposing not an income tax, but an excise tax upon the conduct of business in a corporate capacity, measuring, however, the amount of tax by the income of the corporation, with certain qualifications prescribed by the act itself. *Flint vs. Stone-Tracy Co.*, 220 *U. S.*, 107; *McCoach vs. Minehill Co.*, 228 *U. S.*, 295; *United States vs. Whitridge* (decided at this term, ante, p. 144)."

It is idle to try to sustain the additional income tax we have in hand as an excise; it must be sustained as an income tax or not at all. Even if it was in form an excise it would still be a direct tax on real and personal property, and void.

As strong as the authorities are that the territorial uniformity required by the constitution does not prohibit Congress from discriminating as between persons and things in levying duties, imposts and excises, we are not prepared to admit that there are no limitations on this power.

Suppose Congress in a tariff law should lay a duty of 25 per centum, on the value of wool when imported by an individual and at a less rate, or not at all, when imported by a corporation? The power to tax, or to lay any other public charge, implies some fairly reasonable basis of apportionment. An utterly vicious and flagrant departure from a reasonably just and uniform apportionment would not be within the power granted, but beyond it.

In levying taxes, duties, imposts and excises Congress can make as many classes as it pleases, but there must be something more than mere arbitrary criteria to distinguish the classes from each other.

The tax on the manufacture of beer is an excise, but suppose Congress should enact that when made by an individual the tax should be $2.00 a barrel, but when brewed by a corporation it should be $1.00 a barrel only.

TORN

Or, suppose Congress should enact that individuals and corporations manufacturing not exceeding 20,000 barrels of beer annually should pay a tax of $1.00 a barrel, but individuals brewing more than 20,000 barrels a year should pay an additional tax on the excess of $1.00 a barrel, and corporations brewing more than 20,000 barrels a year should not pay an additional tax on the number of barrels in excess of 20,000.

There are some limitations on the power to tax which are inherent in the forms of constitutional government which prevail in the United States and in the nature of our institutions; in the very words, "taxes, duties, imposts and excises."

Justice Miller, in his "*Lectures on the Constitution of the United States,*" at p. 241, referring to the provisions of state constitutions for uniformity of taxation, said:

> "This has been productive of some trouble. A state might wish to tax whiskey and tobacco higher than a plough or corn field; and this might be prevented by confining the meaning of this language within too narrow bounds. The difficulties in the way of this construction have, however, been very largely obviated by the word 'uniform' which has been adopted, holding that the uniformity must refer to articles of the same class. That is, different articles may be taxed, at different amounts, provided the rate is uniform on the same class everywhere, with all people and at all times.
>
> "Take, for instance, the case of a license. If everybody in any particular class is required to pay a certain license—if lawyers are taxed $25.00 a year, if all merchants are taxed $100 a year, if all saloonkeepers are taxed $200 a year—then it is uniform because it imposes the same burden upon every man of the same class, and who come within the circle of its well defined limits."

Justice Miller was one of the judges of the Supreme Court of the United States who was of the opinion that a tax assessed upon incomes was an excise, *Id., p.* 238; but his death prevented him from participating in the case in which it was authoritatively determined that the income tax of 1894 was a direct tax. If he had been alive, his vote would have been the same as those of Justices Harlan, Brown, Jackson and White, and the authoritative decision would have sustained the income tax of 1894 as a valid excise.

RN PAGES

Chief Justice White is the only judge now a member of the Supreme Court of the United States who participated in that case, and while it is possible for the court to overrule the decision that was made, it is not likely, if we are to judge by what has been said for the court by Mr. Justice Day and Mr. Justice Pitney in the corporation tax cases cited above.

The income tax of 1894 was a flat and uniform rate of two per centum without any graduation or surtaxes. The income tax law of 1913 levies a flat and uniform rate of one per centum, and in this particular is constitutional and valid.

In addition to the normal tax of one per centum, it levies a graduated surtax on the incomes of individuals exceeding $20,000. The validity of the surtax is the question in this case.

Justice Miller wrote the opinion of the court in *Loan Association vs. Topeka*, 20 *Wall*, 655, in which it was held that there is an *implied limitation* in the power to tax that taxes can only be levied for public purposes, and a tax levied for private purposes is unconstitutional.

The power of taxation is a part of the legislative power; it is included in any general grant of that power; and it is subject to the same implied and inherent limitations.

The power to levy taxes does not mean that the government has a right to make indiscriminate seizures of money or property to support itself or to carry on its operations. Such seizures would be regarded as confiscation, unless the government making them paid a just compensation to the owners of the property taken. The line of demarkation which separates confiscation from taxation is that a tax is imposed upon those who have to contribute to it, according to some basis of apportionment, and the compensation for the money paid is the benefit derived by the taxpayer from the protection afforded to him by the government; that is to say, a tax implies some sort of rating by which the several amounts to be paid by the taxpayers are determined.

The legislative authority can not arbitrarily determine what each taxpayer must pay, and it can not confer any such absolute discretion upon any officer of the government.

Some rule of uniformity and equality is therefore absolutely essential to any valid taxation.

There were no express provisions in the constitution of Kentucky on the subject of taxation until 1875, yet the Court of Appeals of that state held that the power of taxation was not unlimited.

In *Sutton's Heirs vs. Louisville*, 5 *Dana (Ky.)*, 28, 31, decided in 1837, the Court of Appeals of Kentucky held a street opening assessment invalid. The first section of the tenth article of the constitution of Kentucky provided "That all freemen, when they form a social compact, are equal, and that no man or set of men are entitled to exclusive separate public emoluments or privileges from the community, but in consideration of public services;" and the twelfth section of the same article declared that no man's property should be taken for public use without just compensation.

The court said:

> "The assessment against the plaintiffs must be considered either as a tax on them or as an appropriation of their property to public use, without their consent; and in either of these aspects of it, can it be sustained as consistent with the constitution?
>
> "If it be a tax, is there no limitation on the power of taxation, and has not some constitutional principle been violated? The State constitution contains no express restriction on the taxing power. *But nevertheless, this power can not be, in all respects, arbitrary and unlimited.*
>
> "The nature and object of taxation, and the spirit of justice and equality which pervades the constitution, and is consecrated by the foregoing first section of the tenth article, necessarily prescribe an impassable boundary to this, which, more than any other legislative power, is constantly exercised and felt, and is always liable to be perverted and abused. And that limit is, *that a common burden should be sustained by common contributions, regulated by some fixed general rule, and apportioned according to some uniform ratio of equality.* Thus, if a capitation or personal tax be levied, it must be imposed on all the free citizens equally and alike, or if an ad valorem or specific tax be laid on property, it must bear equally, according to value or kind, on all the property, or on each article, of the same kind, owned by every citizen; and no citizen or class of citizens, owning any property of the kind subjected to taxation, can be exempted constitutionally on

II.

The provisions of Subdivision 2 of Division A of Section II of the Revenue Act of Congress of Oct. 3, 1913, levying a graduated surtax on the incomes of individuals in excess of $20,000 without levying the same on the incomes of corporations in excess of $20,000 are unconstitutional and void.

The arbitrary, unjust and unwarranted discrimination against individuals and in favor of corporations, resulting from the surtax provisions, will first be demonstrated.

A normal tax of 1 per centum per annum is levied on the net incomes of both individuals and corporations, without any discrimination between them. Dividends actually received by individuals from corporations which have paid the normal tax thereon are deducted from the incomes subject to the normal tax of individuals, showing a clear intention of levying a normal tax of 1 per centum on the actual net gains and profits constituting the incomes of both individuals and corporations. So far the law is intelligible and just.

The provisions putting the dividends actually received from corporations back into the taxable incomes of individuals for the purpose of assessing their surtaxes, may or may not, as a matter of statutory construction, be sustained. We will give the question separate consideration.

Confining the addition (to the income subject to the normal tax) to the dividends actually received does not relieve the surtax on incomes subject to the normal tax of its unjust and unwarranted discrimination against the incomes of individuals and in favor of the incomes of corporations.

An individual with an income of $1,000,000 would pay in addition to the normal tax:

1 per centum on amount between $20,000 and $50,000.....	$ 300
2 per centum on amount between $50,000 and $75,000.....	500
3 per centum on amount between $75,000 and $100,000.....	750

4 per centum on amount between $100,000 and $250,000.....	6,000
5 per centum on amount between $250,000 and $500,000.....	12,500
6 per centum on amount between $500,000 and $1,000,000.....	30,000
	$50,050

A corporation having an income of $1,000,000 distributed among ten equal stockholders would pay to each $100,000, on which the surtax would be:

1 per cent on amount between $20,000 and $50,000.....	$300.00
2 per cent on amount between $50,000 and $75,000.....	500.00
3 per cent on amount between $75,000 and $100,000.....	750.00
	$1,550.00

Multiply by ten and the total amount paid by the stockholders would be $15,500, as compared with the $50,050 an individual would have to pay on an income of $1,000,000.

If there were twenty equal stockholders each would receive $50,000, and the surtax each would pay would only be $300 and the aggregate of their payments would only be $6,000.

If there were fifty equal stockholders each would receive $20,000 and would not pay any surtax at all.

The discrimination is against individuals who are not stockholders in gainful corporations, and in favor of those who are. It is a discrimination as between natural persons by dividing them into two classes, one composed of those who own stock in corporations making gains and profits, and the other consisting of those who do not own any such stock.

There can be no possible excuse or apology for a classification having no other basis. There would be just as much sense in classifying persons for the purpose of taxation by the color of their eyes, or hair, or their weight or height.

If the Secretary of the Treasury does not in any case certify that the undivided and accumulated profits of the corporation are unreasonable for the purposes of the business, such accumulation is not, in assessing the stockholders for their surtaxes, distributed among them, and they escape from surtaxes thereon. The Secretary of the Treasury may or may not certify his opinion.

It is certain, however, that a corporation is entitled to accumulate from its gains and profits a surplus, reasonably necessary for the purposes of its business, and that the amount so accumulated is not to be taken into consideration in computing the surtaxes its stockholders are required to pay.

A corporation makes a profit of say $1,500,000 and pays the normal tax thereon of $15,000.

It only distributes in dividends $1,000,000.

An individual making the like profit of $1,500,000 would pay the like normal tax of $15,000; but he would be required to pay a surtax which would be computed as follows:

1 per centum on amount between $20,000 and $50,000.....	$ 300
2 per centum on amount between $50,000 and $75,000.....	500
3 per centum on amount between $75,000 and $100,000.....	750
4 per centum on amount between $100,000 and $250,000.....	6,000
5 per centum on amount between $250,000 and $500,000.....	12,500
6 per centum on amount between $500,000 and $1,500,000.....	60,000
	$80,050

A corporation making a profit of $1,500,000 accumulates in surplus one-third of it, reducing the distribution to its stockholders to $1,000,000.

If there were ten stockholders holding equal amounts they would receive $160,000 each, and their surtaxes would be computed as follows:

1 per centum on amount between $20,000 and $50,000.....	$ 300
2 per centum on amount between $50,000 and $75,000.....	500
3 per centum on amount between $75,000 and $100,000.....	750
	$1,550

Multiply by ten and the total amount they would pay would be $15,500 as compared with the $80,050 the single individual would pay.

If the Secretary of the Treasury should certify that in his opinion the accumulation of $500,000 was more than was reasonably necessary and the *whole amount* of the gains and profits of the corporation should be taken into consideration, the result would be nearly as bad. The discrimination would still be very marked and distinct.

If there were ten stockholders holding equal amounts they would each be chargeable with $150,000 and their surtaxes would be computed as follows:

1 per centum on amount between $20,000 and $50,000.....	$ 300
2 per centum on amount between $50,000 and $75,000.....	500
3 per centum on amount between $75,000 and $100,000.....	750
4 per centum on amount between $100,000 and $150,000.....	2,000
	$3,500

Multiply by ten and the total is $35,000 as compared with the $80,050 the single individual would pay.

If there were a large number of equal stockholders the aggregate of their payments would be less.

All of which makes it very plain that permitting corporations to accumulate as surplus a portion of their gains and profits, and not permitting individuals to do so, is a vexatious and burdensome discrimination wholly without a redeeming feature.

Many corporations accumulate one-half and even more of their net gains and profits as surplus, to enable them to have the working capital necessary to continue making gains and profits. In the illustration given above, the corporation only retained as surplus one-third of its gains and profits, but in many corporations a much larger proportionate amount is accumulated.

It is not possible to hold that this discrimination is in accord with the principles governing the classification of persons and things for the purposes of taxation.

A corporation is a combination of persons and capital, for the purpose of enabling it to act as a unit, in the conduct of its business, and to do what none of its stockholders could do or would be willing to do, single-handed, with his own limited means and energy.

As far as making gains and profits are concerned, corporations as artificial persons belong to the same class as natural persons, and it is a perfectly plain proposition that in taxing incomes as such, artificial and natural persons must be treated alike, and without discrimination as between the one and the other.

The main discrimination against individuals is that they are required to pay surtaxes, and corporations are not required to do so.

And this discrimination is intensified and made more distinct by the scheme of levying surtaxes on the stockholders of corporations computed on the corporate gains and profits, whether divided or distributed or not.

1. Our first objection to the surtax provisions of the income tax law of Oct. 3, 1913, is that they are in conflict with the provisions that

> "Representatives *and direct taxes* shall be apportioned among the several states which may be included within this Union, according to their respective numbers," etc.
>
> "No capitation or other direct tax shall be laid unless in proportion to the census or enumeration hereinbefore directed to be taken."

They are still a part of the constitution with the construction placed upon them by the Supreme Court of the United States in the *Pollock vs. Farmers' Loan and Trust Co.*, 158 U. S., 601.

That decision was authoritative and final.

The Sixteenth Amendment recognizes it as a permanent interpretation of the constitution; and it is not thinkable the court would now overrule it, and throw the whole subject into chaos.

These constitutional provisions, therefore, as so expounded are in force, except as modified by the Sixteenth Amendment, authorizing Congress to levy taxes on incomes, from whatever source derived, without apportionment among the States according to population.

Congress cannot now, any more than before the Sixteenth Amendment, levy direct taxes on real or personal property unless they are apportioned among the several states according to their respective numbers.

The Sixteenth Amendment and the provisions quoted above must be construed together.

The Sixteenth Amendment did not strike out the words "and direct taxes" "or other direct tax." If that had been the intention the amendment would have been made to read:

> "Congress shall have power to levy and collect *direct taxes* without apportionment among the several States and without regard to any census or enumeration."

Congress can levy taxes on the gains and profits of persons and corporations as long as the levy is on such gains and profits as income, and not upon the sources of the gains and profits.

This absolutely precludes any classification (for the purposes of an income tax) based upon differences in the sources of the incomes.

Thus, real property and personal property as sources of income cannot be divided into two classes and a different rate imposed on the one than on the other.

456,662.67. Having need of more money for the support of the government, Congress makes an additional levy on individuals in the form of surtaxes amounting to $15,525,496.83, which is in excess by the sum of $10,818,887.55 of the sum individuals would have to pay if the rate of the normal tax had been increased one-third of one per cent, with the result that corporations escape their just burden to that amount.

Could any apportionment be more vicious or more in violation of the rule that in all taxation there must be a distribution of the common burdens on some basis having at least the appearance of equality and uniformity.

The law reports abound with cases concerning what is and what is not a public purpose, but there are no cases which hold that an ordinary business corporation, such as a trading or manufacturing company, can be assisted or encouraged with contributions from the public treasury.

And it has been well held that taxes cannot be levied, or money in the treasury be appropriated, for the relief of taxpayers.

In 1836 the United States distributed a surplus of revenue among the states, and they distributed it among their townships and municipalities.

The township of Granville, Mass., in 1849, voted that the interest of the surplus revenue deposited with it should apply in payment of the poll-taxes of the male inhabitants thereof, and the collector to deduct from the poll-tax of the persons assessed the sum of sixty cents upon each of said taxes, and in 1850 the town voted to abate and remit fifty-eight cents of each poll-tax.

In *Cooley vs. Inhabitants of Granville*, 10 *Cush.*, 53, it was held by the court, Chief Justice Shaw presiding,

> "that for the purpose of abating taxes, especially a particular class of taxes, towns cannot raise money by taxation; that consequently the interest of the surplus revenue can not be lawfully appropriated, and that therefore the bill should be sustained and the injunction made perpetual."

The township of Biddeford, Me., voted to distribute the money "among the inhabitants of the town according to

families," meaning according to the number of persons in each family. Held an illegal appropriation of the money. *Hooper vs. Emery*, 14 *Me.*, 375.

A New Jersey law provided:

> "That where a number of school districts are consolidated, an assessment equal to one-fifth of the value of the school property in each of the old districts shall be levied upon all the taxpayers of the consolidated district, and there shall be remitted to the taxpayers of each school district as it existed on the 30th day of June, 1894, one-fifth of the appraised value of the school property belonging to said district, and yearly thereafter one-fifth shall be so assessed and remitted until the whole appraised value is remitted. Held, that this legislation is unconstitutional. It provides for no public necessity or exigency; the tax is not to be appropriated to the expenses of government; its sole end and design is to benefit one class of citizens at the expense of another." *Water Co. vs. Wade*, 59 *N. J. L.*, 78.

In *Weeks vs. Milwaukee*, 10 *Wis.*, 242, a city ordinance exempted the lots on which the Newhall House, of the value of $150,000 to $200,000, was being erected, from taxation for years 1856 and 1857,

> "in view of the great public benefit which the construction of the hotel would be to the city."

Held unconstitutional.

Brewer Brick Co. vs. Brewer, 62 *Me.*, 62, is a case where the annual town meeting voted to exempt from taxation for ten years manufacturing and refining establishments hereafter erected and the capital used for operating the same, provided that the capital invested was not less than $10,000.

Held unconstitutional.

Congress has not as much right to levy a tax for private purposes as has the legislature of a state whose constitution has no provision on the subject, for the clause of the constitution of the United States conferring the power of taxation on Congress carefully limits the power

N PAGES

> "to pay the debts and provide for the common defense and the general welfare of the United States."

That phrase is equivalent of the words of the Statute *Confirmationes Chartarum,* by which Edward I in 1297 promised he would not

> "take such manner of aids, tasks, nor prises, but by the common assent of the realm, and for the common profit thereof."

Coke, commenting thereon, said:

> "But at this parliament this branch gave satisfaction to all, for hereby it is enacted that every aid and task and other taking must have two special properties, the one in the creation, viz., that it be given by the common consent of the whole realm in parliament; and the other in the execution, viz., that it be given and employed for the common benefit of the whole realm, and not for private or other respects."

III.

Classifying incomes according to their sources and levying different rates on the several classes has objectionable features and consequences which do not pertain to that classification which is permissible in levying duties, imposts and excises.

Custom duties and imposts on exports being prohibited by the constitution, they are in the United States confined to importations from foreign countries, but they are required to be uniform throughout the United States.

This territorial uniformity prevents classifications designed to favor certain articles or certain sections of the country from becoming odious. Our tariff laws were at first advantageous to the great manufacturing states of New England, New York and Pennsylvania, but the result was that manufacturing sprang up in the west and the south and all over the country.

The tariff on sugar was of great benefit to the sugar cane growers of the south and the sugar refineries, but it gave birth to the sugar beet industry of the extreme north.

TORN

The tariff shed its beneficent or harmful influence, whichever way you look at it, from one end of the land to the other.

Excises are imposed partly for revenue and partly as police measures to restrain obnoxious callings or to suppress those that are inimical to the objects or policy of the general government, such as the excise on the circulation of state banks of issue; but whatever they are, their operation must be the same throughout the whole country.

Custom duties, imposts and excises have a uniform operation on all in the same class. There can be no favoritism or undue discrimination, for everybody in the same class must be treated alike.

This is not true of income taxes, if incomes can be classified according to the sources from which they are derived and different rates be imposed on the several classes into which they may be divided on the basis of their sources.

Income taxes must be the same on all income taxpayers belonging to the same class.

Income taxes stick where they are laid. Real estate owners and money lenders may reimburse themselves from tenants and borrowers, but they fall remorselessly nevertheless, and if they can be classified according to their different sources, may be the instrument of great partiality and injustice without redeeming feature.

The Constitution says:

> "The Congress shall have power to lay and collect taxes, duties, imposts and excises, to pay the debts and provide for the common defense and general welfare of the United States; but all duties, imposts and excises shall be uniform throughout the United States."

The omission of the word "taxes" in the uniformity clause was probably due to the provisions requiring direct taxes to be apportioned among the states according to population, which would produce a want of uniformity so far as the proportion of the property and wealth of the several states differed from their population.

RN PAGES

Literally construed, income taxes are not required to be territorially uniform throughout the United States. We do not think that view is correct, but if it is not, it is because of an implied limitation to the contrary in the Sixteenth Amendment. We do not believe Congress has power to levy an income tax at different rates in the several states, or in groups of states, but if it can classify incomes according to their sources it can resort to discriminations of a more odious and obnoxious nature, and more dangerous because insidious.

Thus, it would be very popular in some quarters at the present time to levy a higher rate on incomes derived from the manufacture or sale of spirituous or fermented liquors.

Another popular discrimination would be a higher rate on the incomes of railroad, street railway and other public service corporations.

A still more popular discrimination would be a higher rate on the incomes of oil and steel and automobile corporations.

And just before each congressional or presidential election the demand for a lower rate on incomes derived from agricultural pursuits would be irresistible.

Another very popular measure would be the adoption of the distinction first enacted in England in 1907 between earned and unearned income, the object of which is to compel those whose incomes are derived from saved or inherited property to pay a higher tax than those whose incomes are derived from personal earnings or from business.

There is no limit to the discriminations Congress may resort to if it can classify incomes on the basis of the sources from which they are derived.

What we contend for is that Congress has no such power, and that its power to graduate the tax is quite sufficient to reach the more wealthy classes.

On the authority of *Magoun vs. Illinois Trust and Savings Bank*, 170 *U. S.*, 283, we assume, for the purposes of this case, that Congress can levy a graduated income tax. The appellants make no objection on that ground.

With a normal rate of one per cent, or any other normal

TORN

rate Congress may levy, the higher the income the higher *tax*, and that would seem to be all sufficient to reach the rich, but it may be good policy to enact that the higher the income the higher the *rate*.

What appellants object to is classifications and discriminations based on the sources from which the taxable incomes are derived.

A graduated tax on inheritances was sustained because it was a tax on the privilege of inheritance accorded by the law, and was not a tax on the property inherited.

A graduated tax on incomes can be sustained because it is a tax on incomes and not a tax on the property or other sources from which the incomes are derived.

The distinction is plainly discernible, but if incomes can be classified according to their sources for the purposes of taxation, the distinction is not discernible, for it ceases to exist.

IV.

The additional assessment of $13,216.50 against each of the appellants was not authorized by the act, and they are entitled to recover $26,433, even if the surtax assessed on their incomes subject to the normal tax is constitutional.

This question requires a construction of the provision which reads:

> "For the purpose of such additional tax the taxable income of any individual shall embrace the share to which he would be entitled of the gains and profits, if divided or distributed, whether divided or distributed or not, of all corporations, joint stock companies or associations, however created or organized, formed or fraudulently availed of *for the purpose of preventing the imposition of such tax* through the medium of permitting such gains and profits to accumulate instead of being divided or distributed," etc.

We contend that unless a corporation was "created, organized, formed or fraudulently availed of," for the purpose of defeating the tax, none of the gains and profits, whether di-

ORN PAGES

vided or distributed or not, are to be added to the incomes subject to the normal tax of individual stockholders.

In other words, that neither the dividends actually received or the shares of the undivided gains and profits are to be included unless the corporation was "created, organized, formed or fraudulently availed of" for the purpose indicated.

A corporation pays the normal tax on all its gains and profits, including such part thereof as it distributed in dividends, and the evident meaning of the provision in question is that there is to be no transfer of this income to the individual stockholders, unless the corporation was "created, organized, formed, or fraudulently availed of."

The bill of complaint in this cause distinctly alleges:

> "That the plaintiffs have been informed and believe and charge the fact to be that the corporation from which they received said dividends was not "created or organized, formed or fraudulently availed of for the purpose of preventing the imposition of such tax through the medium of permitting such gains and profits to accumulate instead of being divided and distributed." (*Record, p.* 17.)

The protest set forth in the supplemental bill distinctly claims

> "That a part of said surtaxes, to wit: $13,216.50, upon an alleged taxable income of $220,275.00 is not authorized by said Subdivision 2 of Division A of the [illegible],"

and the prayer is

> "for a prompt and speedy decree against the defendant for the amounts so paid by them." (*Record, pp.* 37-38.)

The dividends received amounted to $216,941.66 and without any warrant in the law for it, the Commissioner added the statutory exemption of $3,333.34, making a total of $220,275.00.

We respectfully submit that if Subdivision 2 of Division A of the Income Tax Law of Oct. 3, 1913, is sustained as constitutional, nevertheless the assessment of $13,216.50 against each of appellants is not within the statute, and the appellants are entitled to a judgment for the recovery of $26,433.00 with interest and costs.

On the whole case we contend that the appellants are entitled to a decree declaring the surtax provisions of the act unconstitutional, and to a judgment against the collector under section 3220 of the Rev. Stat, for the entire amount paid by them, $91,581.37 with interest and costs.

The decree below should be reversed and the case remanded with directions to the court below to enter such a decree or judgment.

This brief is not what it should be, but I have endeavored to state the case fairly and accurately, and to make an intelligible presentation of the questions raised and relied on.

FRED A. BAKER,
Counsel for Appellants.

any other ground than that of valuable and peculiar public services—for otherwise one man, or a 'set of men,' might be entitled to enjoy 'exclusive privileges,' or legal exemptions, which are substantially the same, without the only constitutional consideration of public services."

In *Lexington vs. McQuillan's Heirs*, 9 *Dana* (*Ky.*), 513, decided in 1840, the court made these observations:

"When shall a tax be levied? to what amount? Shall it be a capitation or property tax? Direct or indirect? Ad valorem or specific? And what classes of property are the fittest subjects of taxation?—are all questions wisely confided by our constitution to the discretion of the legislative department, subject to no other limitation than that of the moral influence of public virtue, and responsibility to public opinion?

"But in some other respects, and so far as the power of taxation may be effectual without being thus limited, it is, in our judgment, *limited by some of the declared ends and principles of the fundamental law*. Among these political ends and principles, equality, as far as practicable, and security of property against irresponsible power, are eminently conspicuous in our State constitution. An exact equalization of the burden of taxation is unattainable and utopian. *But still there are well defined limits within which the practical equality of the constitution may be preserved, and which, therefore, should be deemed impassable barriers to legislative power.* Taxation may not be universal, but it must be general and uniform. Thus, if a capitation tax be laid, none of the class of persons thus taxed can be constitutionally exempt upon any other ground than that of public service; and, if a tax be laid on land, no appropriation land within the limits of the state can be constitutionally exempted, unless the person be entitled to such immunity in consequence of public service. The legislature, in the plentitude of its taxing power, *can not have constitutional authority to exact from one citizen, or even one county, the entire revenue for the whole commonwealth.*

"Such an exaction, by whatever name the legislature might choose to call it, would not be a tax, but would be undoubtedly the taking of private property for public use, and which could not be done constitutionally with-

TORN PA

out the consent of the owner or owners, or without retribution of the value in money.

"The distinction between constitutional taxation and the taking of private property for public use by legislative will may not be definable with perfect precision. But we are clearly of the opinion that whenever the property of a citizen shall be taken from him by the sovereign will, and appropriated, without his consent, to the benefit of the public, the exaction *should not be considered as a tax, unless similar contributions be made by that public itself, or shall be exacted rather by the same public will, from such constituent members of the same community generally* as own the same kind of property. Taxation and representation go together. And representative responsibility is one of the chief conservative principles of our form of government.

"When taxes are levied, therefore, they must be imposed on the public in whose name and for whose benefit they are required, and to whom those who impose them are responsible. And, although there may be a discrimination in the subjects of taxation, *still persons in the same class, and property of the same kind, must generally be subjected alike to the same common burden. This alone is taxation, according to our notion of constitutional taxation in Kentucky.* And this idea, fortified by the spirit of our constitution, is, in our judgment, confirmed by so much of the twelfth section of the tenth article as declares, 'Nor shall any man's property be taken or applied to public use without the consent of his representatives, and without just compensation being previously made to him.'

"The object of this great guarantee was to secure every citizen against *spoliation by a dominant faction, or by a rapacious public power*, acting in obedience to the will of a constituent body for whose use his property may be taken, and from whom no similar contribution is required. It intended that public responsibility, and the power of exaction for public use, should be, in some degree, commensurable; and, therefore, it should be understood as providing that the public shall not take the property of any citizen for its own use, without his consent, or an equivalent in money, or in similar contributions by itself.

"If this be not its practical effect, it is mere *brutum*

fulmen, and may always be evaded by exactions made in the false semblance of taxation."

In 1871 the Kentucky Court of Appeals held a street paving assessment unconstitutional.

Howell vs. Bristol, 8 *Bush*, 493.

The court said:

> "A law imposing taxation on the general public, the evident intent and legitimate result of which is to equalize the burden, so far as practicable, will not be held as violative of the fundamental law merely because that desirable end may not be attained. But when, as in this case, the *most probable, if not the necessary, consequence of the law is to produce the most oppressive inequality, and to compel a small minority of taxpayers to provide, at their sole expense, an improvement of general utility* and public interest, the construction of which costs more than double as much as the character of such improvements in general use, and from which, when constructed, the general public derives almost as much advantage as themselves, *it assumes the character of an attempted exercise of 'arbitrary power' over the property of this minority; it becomes, in the constitutional sense, a taking and appropriation of their private property to the public use without compensation*, and it can not be sustained so long as the safeguards placed around the citizen by our fundamental law are respected and upheld. No such power over the property of the citizen can be constitutionally exercised by any department of our state government; and whenever it is attempted it is the imperative duty of the judiciary to interpose in behalf of those whose constitutional rights are being thereby prejudicially affected."

The Kentucky court was perfectly logical in calling attention to the provision of the State constitution that no man's property should be taken for the public use without compensation; but it might have further said that to take a man's property without compensation was also a violation of the provision of the State constitution against depriving a person of his property without due process of law, or as expressed in the constitution of Kentucky, "unless by the judgment of his peers or the law of the land."

The Supreme Court of the United States has held that the due process of law clause of the Fourteenth Amendment forbids the states from taking private property for the public use without compensation, or for private use at all. (*Chicago, etc., R. Co. vs. Chicago*, 166 *U. S.*, 226; *Norwood vs. Baker*, 172 *U. S.*, 269; *Missouri Pac. R. Co. vs. Nebraska*, 164 *U. S.*, 403, 417.)

This makes it apparent that the requirement of due process of law does restrain the power of taxation, and that a tax law in order to be valid must so distribute the public burden as to have some degree of uniformity and equality, some basis of apportionment sufficiently equitable, to give the imposition the character of a tax levied for public purposes.

Before New Jersey had an express constitutional provision requiring uniformity of taxation the Supreme Court of that state, in the case of *State vs. Township Committee of Readington*, 36 *N. J. L.*, 66, said:

> "The power of the legislature in the matter of taxation is said to be unlimited. Such undoubtedly is the theory of our government. But it is not every exaction made under color of taxation that can be supported as the legitimate exercise of the sovereign power of taxation. *It is of the very essence of taxation that it should be equal and uniform, and that where the burden is common there should be a common contribution to discharge it. Cooley's Const. Law*, 495. Not that it is essential to the validity of taxation that it should be levied according to rules of abstract justice. The legislature may create special taxing districts, defining their limits in its discretion, or designate certain occupations, trades or employments as special subjects for taxation; or discriminate between different kinds of property in the rate of taxation; or may apportion the tax among the classes of persons or property made liable to taxation, in such manner as may seem fit. In this way inequalities in the share of the public burden, or even double taxation, may arise without any relief except by appeal to the legislature. *But when the taxing district has been defined, and the classes of persons or kind of property* specially set apart for taxation have been designated, the tax must be apportioned among those who are to bear the burden upon the rule of uniformity. *Cooley's Const. Law, pp.* 493-513. Taxation

operates upon a community, or a class in a community, *according to some rule of apportionment*. When the amount levied upon individuals is determined without regard to the amount or value exacted from any other individual or classes of individuals, the power exercised is not that of taxation, but of eminent domain. *The People vs. Mayor of Brooklyn*, 4 *Comstock*, 420. A tax upon the persons or property of A, B and C individually, whether designated by name or in any other way, which is in excess of an equal apportionment among the persons or property of the class of persons or kind of property subject to the taxation, is, *to the extent of such excess, the taking of private property for a public use without compensation. The process is one of confiscation and not of taxation.*"

New York has never had any constitutional provision securing uniformity of taxation, and the Court of Appeals of that state has regarded the power of the legislature over the subject of taxation as almost unlimited.

People vs. Brooklyn, 4 *N. Y.*, 420.

But the opinion of the court in that case distinctly affirms, p. 424, that "Taxation operates upon a community, or upon a class of persons in a community, and *by some rule of apportionment;*" and further on, p. 427, "The power of taxing and the power of apportioning taxation are identical and inseparable. *Taxes cannot be laid without apportionment;* and the power of apportionment is therefore unlimited, unless be restrained as part of the power of taxation."

The constitution of Connecticut contains no express limitation on the power of taxation, and the Supreme Court of that state has gone farther in sustaining an unlimited power in the legislative authority over the subject of taxation than any other court in the United States.

State vs. Travelers' Ins. Co., 73 *Conn.*, 255.

Yet the opinion of the court on that question concludes as follows:

"Is it so, then, that the legislature may make any exaction it pleases under the form of a tax? Clearly not. The legislative power in all its manifestations is limited, including that of taxation, which, however,

from its inherent nature, approaches more nearly to arbitrary power. If a tax is laid on the exercise of the duty of voting, or if *any exaction is put in the form of taxation as a mere sham*, and is in effect and purpose a denial to one of the enjoyment of rights indicated in the constitution and the enjoyment of which it secures equally to all, or *is a seizure of the property of one for the benefit of another, or is an uncompensated confiscation of property*, the law authorizing such exaction is in violation of mandates contained in our constitution, and probably in all American constitutions, and is therefore void. It is neither taxation nor legislation."

We have quoted from the opinions of the courts in these Kentucky, New Jersey, New York and Connecticut cases because we think they lay down the correct doctrine.

We submit that the words "taxes on incomes" as used in the Sixteenth Amendment carry of themselves two limitations on the power of Congress: (1) That the burden be confined to incomes *as such*, and (2), that it must be apportioned on some basis of equality and uniformity, and not arbitrarily or capriciously.

The income tax law of Oct. 3, 1913, itself furnishes all the criteria needed to invalidate its surtax provisions.

1. Natural persons, and corporations as artificial persons, are both put in the same class of income taxpayers, and a uniform rate imposed of 1 per cent per annum on their net incomes from whatever source derived. *This fixes their status as taxpayers, and makes both of them members of the same class.*

2. The surtax provisions make a violent and highly obnoxious discrimination between members of the same class, in that some of the same class are required to pay an enormously higher rate in the form of graduated surtaxes. *Southern Railway Co. vs. Greene*, 216 *U. S.* 400, *and cases cited on p.* 417.

APPORTIONMENT.

Congress levies a normal tax on incomes of 1 per centum, which produced from individuals during the first ten months of its operation $12,728,038.02, and from corporations $32,-

affirms the judgment which put an end to an absolutely useless controversy.

Brushaber v. *Union Pac. R. R. Co., ante*, p. 1, followed to effect that the Income Tax Law of 1913 is not unconstitutional in any of the respects involved in that or this action.

THE facts, which involve the constitutionality and application of the Income Tax Law of 1913, are stated in the opinion.

Mr. William D. Guthrie, with whom *Mr. Fred A. Baker* was on the brief, for appellant:

The whole of the Income Tax provision of the Tariff, subd. 2, div. A, of § 2 of the Act of October 3, 1913, is unconstitutional, because of the invalidity of the provisions: (1) subjecting stockholders in corporations, when computing their surtaxes to liability for the gains and profits of the corporations which have not been divided or distributed; (2) vesting in the Secretary of the Treasury an arbitrary power of determining, without notice, or a hearing, whether any corporation has accumulated a greater undivided surplus than is reasonable for the needs and purposes of the business; and (3) permitting corporations to accumulate and withhold from surtax taxation such part of their gains and profits as may be reasonably necessary for the needs and purposes of the business, and in not according such great business privilege to individuals and partnerships.

The provisions levying a graduated surtax on the incomes of individuals in excess of $20,000 without levying the same on the incomes of corporations in excess of $20,000 are unconstitutional and void.

Classifying incomes according to their sources and levying different rates on the several classes has objectionable features and consequences which do not pertain to that classification which is permissible in levying duties, imposts and excises.

In support of these contentions, see *Brewer Brick Co.* v. *Brewer*, 62 Maine, 62; *Chicago &c. R. R.* v. *Chicago*, 166 U. S. 226; *Coe* v. *Armour Fertilizer Works*, 237 U. S. 413; *Cooley* v. *Granville*, 10 Cush. 53; *DeBarry* v. *Dunne*, 162 Fed. Rep. 961; *Flint* v. *Stone Tracy Co.*, 220 U. S. 107; *Georgia R. R.* v. *Wright*, 207 U. S. 127-138; *Grier* v. *Tucker*, 150 Fed. Rep. 658; *Howell* v. *Bristol*, 8 Bush, 493; *Hooper* v. *Emery*, 14 Maine, 375; *Lexington* v. *McQuillan*, 9 Dana (Ky.), 513; *Loan Association* v. *Topeka*, 20 Wall. 655; *Louis. & Nash. R. R.* v. *Stock Yards* 212 U. S. 132, 144; *McCoach* v. *Minehill Co.*, 228 U. S. 295; *Mo. Pac. Ry.* v. *Nebraska*, 164 U. S. 403, 417; *Norwood* v. *Baker*, 172 U. S. 269; *People* v. *Brooklyn*, 4 N. Y. 420; *Pollock* v. *Farmers' L. & T. Co.*, 158 U. S. 601; *Roller* v. *Holly*, 176 U. S. 398, 409; *Schwerzchild* v. *Rucker*, 143 Fed. Rep. 656; *Sears* v. *Cottrell*, 5 Michigan, 251; *Security Trust Co.* v. *Lexington*, 203 U. S. 323, 333; *State* v. *Township*, 36 N. J. L. 66; *State* v. *Travellers' Ins. Co.*, 73 Connecticut, 255; *Southern Ry.* v. *Greene*, 216 U. S. 400, 417; *Stratton's Independence* v. *Howbart*, 231 U. S. 414; *Stuart* v. *Palmer*, 74 N. Y. 183, 188; *Sutton* v. *Louisville*, 5 Dana (Ky.), 28, 31; *United States* v. *Whitridge*, 231 U. S. 144; *Weeks* v. *Milwaukee*, 10 Wisconsin, 242; *Water Co.* v. *Wade*, 39 N. J. L. 78.

The Solicitor General and *Mr. Assistant Attorney General Wallace* for appellee.[1]

Mr. Chief Justice White delivered the opinion of the court.

The appellants are the same persons who sued in *Dodge* v. *Osborn*, just decided, *ante*, p. 118. After the dismissal of that suit by the Supreme Court of the District of Columbia for want of jurisdiction the parties, on June 10, 1914, filed their bill in the court below against the Collector

[1] For abstract of argument in this and other cases argued simultaneously herewith, see p. 5, *ante*.

of Internal Revenue to enjoin the collection of the surtaxes assessed against them which were disputed in the previous case on substantially the same grounds alleged in the complaint in that case. The bill alleged, however, that plaintiffs had filed with the Collector "an appeal or claim for the remission and abatement of the surtaxes" because of the unconstitutionality of the statute imposing them and that the Commissioner of Internal Revenue to whom the claim had been forwarded by the Collector had such protest under advisement. Upon the filing of the bill the plaintiffs moved for a preliminary injunction which was denied July 29, 1914. On the same day by leave of court a supplemental bill was filed which alleged that since the filing of the original bill the Commissioner of Internal Revenue had ruled adversely upon plaintiffs' protest and that thereupon they had paid the surtaxes to the Collector under protest, and they prayed a recovery of the amount paid to the Collector and for the other relief asked in the original bill. The defendant moved to dismiss the bill for want of jurisdiction because the suit was brought to enjoin the collection of a tax contrary to the provisions of Rev. Stat., § 3224, and for want of equity because the Income Tax Law was constitutional and valid. The court sustained the motion on the latter ground and dismissed the bill on the merits and the case is here on direct appeal because of the constitutional questions.

The Government insists that the court below was without jurisdiction to decide the merits and we come first to that question. It is apparent if the original bill alone is taken into view that the suit was brought to enjoin the collection of a tax and the court was without jurisdiction for the reasons stated in the previous case. And it is argued by the Government that there was no jurisdiction under the supplemental bill since it fails to allege that an appeal was taken to the Commissioner of Internal Revenue after the payment of the taxes and that he refused

to refund them and therefore fails to allege a compliance with the conditions imposed by §§ 3220 and 3226 of the Revised Statutes as prerequisites to a suit to recover taxes wrongfully collected. But broadly considering the whole situation and taking into view the peculiar facts of the case, the protest to the Commissioner and his exertion of authority over it and his adverse ruling upon the merits of the tax, thereby passing upon every question which he would be called upon to decide on an appeal for a refunding of the taxes paid, we think that this case is so exceptional in character as not to justify us in holding that reversible error was committed by the court below in passing upon the case upon its merits, thus putting an end to further absolutely useless and unnecessary controversy. We say useless and unnecessary because on the merits all the contentions urged by the appellants concerning the unconstitutionality of the law and of the surtaxes which it imposes have been considered and adversely disposed of in *Brushaber* v. *Union Pacific R. R.*, *ante*, p. 1.

Judgment affirmed.

MR. JUSTICE MCREYNOLDS took no part in the consideration and decision of this case.